SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., ET AL., PETITIONERS,

vs.

EMERY C. BLACKWELL, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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[fol. 1] [Caption omitted]

IN THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF TEXAS, BROWNSVILLE DIVISION

Civil Action No. 728

EMERY C. BLACKWELL, et al.,

vs.

LLOYD M. BENTSEN, et al.

[fol. 2] COMPLAINT—Filed June 27, 1951

To the Honorable James V. Allred, Judge of said Court:

Now come Emery C. Blackwell, an individual resident of Hidalgo County, Texas, Boyd Construction Company, a private corporation organized under the laws of the State of Texas, with its principal office in Hidalgo County, Texas, Claude E. Blackwell, an individual resident of Tarrant County, Texas, Clyde W. Weatherly, an individual resident of Hunt County, Texas, Arie K. Smith, Dudley Smith, W. H. Ham, and Herbert Clark, all individual residents of Moore County, Texas, hereinafter called Plaintiffs, complaining of Lloyd M. Bentsen, Sr., Elmer C. Bentsen, G. F. Dohrn, Albert L. Richter, R. B. Kale, Earl Pummill, Carl Pummill, C. W. Norton, C. A. Conner, and L. H. Ramey, all individual residents of Hidalgo County, Texas, O. M. Ohmit, an individual resident of Potter County, Texas, Allen Beckham, an individual resident of Hale County, Texas, Pummill Development Company and Pummill Management Company, both private corporations organized under the laws of the State of Texas, with their principal offices in Hidalgo County, Texas, and Bentsen Development Company, a partnership [fol. 3] composed of Lloyd M. Bentsen and Elmer C. Bentsen, doing business in Hidalgo County, Texas, all hereinafter called Defendants, and would respectfully show the Court the following:

I

This action arises under the Securities Act of 1933, May 27, 1933, c. 38, Title I, #48 Stat. 74, as hereinafter more fully appears.

II

The nature of Plaintiffs' complaints against Defendants is that the Defendants, and each of them, entered into a plan and scheme in the nature of a conspiracy to defraud members of the buying public, and particularly these Plaintiffs, by selling securities and/or investment contracts in violation of Sections 77 1. (2) and 77 q of said Securities Act of 1933. The suit is brought as a class suit on behalf of the plaintiffs herein, as well as all other purchasers similarly situated, not parties to the suit. There are common questions of law and fact involved, which by authority of the Federal Rules of Procedure, allow said suit to be filed jointly by these Plaintiffs.

In carrying out said general plan and scheme, the Defendants acquired title to an 800-acre tract of unirrigated land in Hidalgo County, Texas, prepared it to resemble irrigated citrus land, and sold it in small tracts as irrigated citrus land to Plaintiffs and other members of the buying [fol. 4] public residing outside of the Rio Grande Valley of Texas, and unfamiliar with the true facts, at prices far above its actual value, together with a property management or care contract, the whole transaction being treated as an investment by both buyer and seller. Through said care contracts, Defendants continued to extract money from the Plaintiffs under continuing false and fraudulent representations that representations previously made were true, and that the investment was sound and was appreciating in value through such continuing investment and through affirmative acts of concealment of the true facts. The Plaintiffs also allege and will show the Court that such sales of securities and/or investment contracts were made by false and fraudulent representations and by fraudulent concealment of material facts, and that the same representations and concealment were used in connection with the sales to these Plaintiffs and all other members of the class, not parties to the suit.

Each of the Defendants performed his or its part of said plan and scheme, and did execute and perpetrate said fraud upon these Plaintiffs in connection with certain sales of securities and/or investment contracts executed by Pummill

Development Company and Pummill Management Company as sellers and the Plaintiffs as purchasers.

III

(1) That pursuant to said plan and scheme, the Plaintiff [fol. 5] Boyd Construction Company did on February 24, 1950, purchase said securities and/or investment contracts in the form of a 20-acre tract of land planted to young citrus trees and known as the South One-half (½) of the West One-half (½) of Lot Six (6), Block Twenty-six (26), Rio Grande Development Company's Subdivision, Hidalgo County, Texas, agreeing to pay therefor the sum of $400.00 per acre, or the total sum of $8,000.00 in cash, further paying $2,500.00 in cash to have said land planted to young citrus trees. That since the date of said purchase, said Plaintiff has spent the additional sum of $1,944.25 on the care of said trees and/or investment contract, and has had additional expense in investigating said investment and discovering the true facts in the sum of $630.00. That said purchase contract was executed by Carl Pummill, President or Secretary of Pummill Development Company and Paul J. Boyd of Boyd Construction Company on February 24, 1950, and a warranty deed was subsequently issued to Paul J. Boyd Construction Company dated February 24, 1950, and corrected by a deed dated December 4, 1950, to Boyd Construction Company, said deeds now being of record in Vol. 692, page 464, and Vol. 706, page 573, respectively, of the Deed Records of Hidalgo County, Texas. The Pummill Management Company, on February 24, 1950, also executed and delivered to the said Plaintiff a care contract, by which they agreed to care for the property for five years, [fol. 6] with the Plaintiff to continue to invest money in said property through such care, by depositing sufficient sums from time to time in the First National Bank of Mission, Texas, to the joint account of the Plaintiff and Pummill Management Company. Such investment was to continue during the five-year period of the contract. The aforesaid deeds and care statements, as well as monthly statements on the investment to be made in the care fund, were forwarded to the Plaintiff through the United States Mails. That to the date of this suit, Plaintiff has invested in said

security the sum of $13,074.25, and has had no return of any kind since the purchase of said security and/or investment contract.

(2) That pursuant to said plan and scheme, the Plaintiff Emery C. Blackwell did on November 23, 1949, purchase said security and/or investment contract in the form of a 40-acre tract of land planted to young citrus trees and known as Lot One (1), Block Thirty-one (31), Rio Grande Development Company's Subdivision, Hidalgo County, Texas, agreeing to pay therefor the sum of $400.00 per acre, or the total sum of $16,000.00, paying down the sum of $4,000.00 in cash and executing five notes for $2,400.00 each due annually thereafter bearing interest at the rate of five (5) per cent per annum, and he paid the further sum of $5,000.00 in cash for said citrus trees. That on January 26, 1950, he purchased Lot Twelve (12), Block Twenty-six (26), [fol. 7] of the same subdivision, containing 40 acres, agreeing to pay therefor the sum of $16,000, trading in as the down payment, property owned by the Plaintiff in Pecos, Texas, described as Lots Twenty-four (24), Twenty-five (25) and Twenty-six (26) of Block Forty-three (43), of the N. P. Subdivision to the Town of Pecos, Reeves County, Texas, for the sum of $6,000, and executing five notes for $2,000.00, each due annually thereafter bearing interest at the rate of five (5) per cent per annum. Said Plaintiff has since such purchase spent the additional sum of $4,177.58 on the care of said trees and/or investment contract, and has paid the additional sum of $3,500.00 on the purchase price of said property and $93.97 as taxes on the property. In addition to this, the Plaintiff has spent approximately $200.00 in investigating the investment and finding out the true facts. Said purchase contracts were executed by Carl Pummill, President of Pummill Development Company, and the Plaintiff, Emery C. Blackwell, on November 23, 1949, and January 26, 1950, respectively, and warranty deeds were delivered to the Plaintiff bearing said dates, now of record in Vol. 655, page 373-375 and Vol. 684, page 193-195 of the Deed Records of Hidalgo County, Texas, respectively. The Pummill Management Company purported to care for said property under the terms of its care agreement, and the deeds and bills for care of said investment were forwarded by the Defendants to the Plaintiff through the United

[fol. 8] States Mails. That to the date of this suit, Plaintiff has invested in said security the sum of $22,971.55, and has had no return of any kind since the purchase of said security and/or investment contract.

(3) That pursuant to said plan and scheme, the Plaintiff Claude E. Blackwell did on January 25, 1950, purchase said security and/or investment contract in the form of a 20-acre tract of land planted to young citrus trees and known as the North One-half (½) of Lot Twelve (12), Block Twenty-three (23) of the Rio Grande Development Company's Subdivision, Hidalgo County, Texas, agreeing to pay therefor the sum of $8,000.00, of which amount $2,000.00 was paid in cash and the balance was evidenced by five notes of $1,200.00, each bearing interest at the rate of five (5) per cent per annum, and further paying $2,500.00 in cash for said citrus trees. That since the date of said purchase, the Plaintiff has spent the sum of $1,180.30 on care of said property, $14.18 for taxes, $300.00 interest on said notes, and $230.00 in investigating said investment and discovering the true condition of said property. That said purchase contract was executed by Carl Pummill, President of Pummill Development Company, and Claude E. Blackwell, Plaintiff, on January 25, 1950, and a warranty deed was subsequently issued to the Plaintiff dated January 25, 1950, now of record in Vol. 684, pages 195-197. That on February 15, 1950, the Pummill Management Company executed and [fol. 9] delivered to the said Plaintiff a care contract by which they agreed to care for the property for five years, with the Plaintiff to continue to invest money in said property through such care, by depositing sufficient sums from time to time in the First National Bank of Mission, Texas, to the joint account of the Plaintiff and Pummill Management Company. Such investment was to continue during the five-year period of the contract. The aforesaid deeds and care contract, as well as monthly statements on the investment to be made in the care, were forwarded to the Plaintiff through the United States Mails. That to the date of this suit, Plaintiff has invested in said security the sum of $6,232.48, and has had no return of any kind since the purchase of said security and/or investment contract.

(4) That pursuant to said plan and scheme, the Plaintiff Clyde W. Weatherly and Lois Weatherly, husband and

wife, did on January 28, 1950, purchase said security and/or investment contract in the form of a 20-acre tract of land planted to young citrus trees and known as the North One-half (½) of Lot Twelve (12), Block Thirty-one (31) of the Rio Grande Development Company's Subdivision, Hidalgo County, Texas, agreeing to pay therefor the sum of $7,200.00, and paying $2,700.00 in cash on said land, and executing five notes each in the sum of $900.00, each due annually bearing interest at the rate of five (5) per cent per annum, and further paying the sum of $2,500.00 in cash for said citrus trees. That since the date of said purchase, [fol. 10] they have paid the sum of $1,263.76 for care of said property, $14.18 for taxes, $900.00 in payment of Note No. 1, plus interest of $225.00. They have also spent the sum of $200.00 investigating said investment and finding out the true facts concerning same. That said purchase contract was executed by Carl Pummill as President of Pummill Development Company, and the Plaintiff, Clyde W. Weatherly, and wife, Lois Weatherly, and a warranty deed was subsequently issued to Plaintiff and wife, dated January 28, 1950, and recorded in Vol. 655, pages 482-84 of the Deed Records of Hidalgo County, Texas. That on February 15, 1950, the Pummill Management Company executed and delivered to the said Plaintiff a care contract by which they agreed to care for the property for five years, with the Plaintiff to continue to invest money in said property through such care, by depositing sufficient sums from time to time in the First National Bank of Mission, Texas, to the joint account of the Plaintiff and Pummill Management Company. Such investment was to continue during the five-year period of the contract. The aforesaid deeds and care contract, as well as monthly statements on the investment to be made in the care, were forwarded to the Plaintiff through the United States Mails. That to the date of this suit, Plaintiff has invested in said security the sum of $7,802.94, and has had no return of any kind since the purchase of said security and/or investment contract.

(5) That pursuant to said plan and scheme, the Plaintiff [fol. 11] Arie K. Smith did, on March 3, 1950, purchase said security and/or investment contract in the form of a 20-acre tract of land planted to young citrus trees and known as the South One-half (½) of the West One-half (½) of Lot Seven

(7), Block Twenty-three (23), of the Rio Grande Development Company's Subdivision, Hidalgo County, Texas, agreeing to pay therefor the sum of $8,000.00, paying $4,000.00 in cash down and executing five notes in the sum of $800.00 each, due annually thereafter, bearing interest at the rate of five (5) per cent per annum, and further paying the sum of $2,500.00 in cash for said citrus trees. That since said purchase, the Plaintiff has paid the sum of $1,537.60 for care for said trees, $14.18 for taxes, and $4,048.00 in advance in cash as the balance of the purchase price plus interest, and an additional $200.00 in investigating the investment and discovering the true facts concerning said investment. That said purchase contract was executed by Carl Pummill as President of Pummill Development Company and the Plaintiff, Arie K. Smith, and a warranty deed to said property was subsequently issued to Plaintiff dated March 3, 1950, now of record in Vol. 694, page 360-62 of the Deed Records of Hidalgo County, Texas. That on April 7, 1950, the Pummill Management Company executed and delivered to the said Plaintiff a care contract by which they agreed to care for the property for five years, with the Plaintiff to continue to invest money in said prop- [fol. 12] erty through such care, by depositing sufficient sums from time to time in the First National Bank of Mission, Texas, to the joint account of the Plaintiff and Pummill Management Company. Such investment was to continue during the five-year period of the contract. The aforesaid deeds and care contract, as well as monthly statements on the investment to be made in the care, were forwarded to the Plaintiff through the United States Mails. That to the date of this suit, Plaintiff has invested in said security the sum of $12,299.78, and has had no return of any kind since the purchase of said security and/or investment contract.

(6) That pursuant to said plan and scheme, the Plaintiff Dudley Smith, did on March 3, 1950, purchase said security and/or investment contract in the form of a 20-acre tract of land known as the North One-half (½) of the West One-half (½) of Lot Seven (7), Block Twenty-three (23), Rio Grande Development Company's Subdivision, Hidalgo County, Texas, agreeing to pay therefor the sum of $8,000.00, paying $2,700.00 in cash down and executing

five notes in the sum of $1,060.00, each due annually thereafter bearing interest at the rate of five (5) per cent per annum, and further paying the sum of $2,500.00 in cash for said citrus trees. That since said purchase, the Plaintiff has paid the sum of $1,309.70 for care for said trees, $14.18 for taxes, and $1,325.00 in payment of Note No. 1, plus accrued interest, and an additional $200.00 in investigating [fol. 13] the investment and discovering the true facts concerning said investment. That said purchase contract was executed by Carl Pummill as President of Pummill Development Company, and the Plaintiff, Dudley Smith, and a warranty deed to said property was subsequently issued to Plaintiff dated March 3, 1950, and now of record in the Deed Records of Hidalgo County, Texas. That on April 7, 1950, the Pummill Management Company executed and delivered to the said Plaintiff a care contract by which they agreed to care for the property for five years, with the Plaintiff to continue to invest money in said property through such care, by depositing sufficient sums, from time to time, in the First National Bank of Mission, Texas, to the joint account of the Plaintiff and Pummill Management Company. Such investment was to continue during the five-year period of the contract. The aforesaid deeds and care contracts, as well as monthly statements on the investment to be made in the care, were forwarded to the Plaintiff through the United States Mails. That to the date of this suit, Plaintiff has invested in said security the sum of $8,048.88, and has had no return of any kind since the purchase of said security and/or investment contract.

(7) That pursuant to said plan and scheme, the Plaintiff W. H. Ham did on March 3, 1950, purchase said security and/or investment contract in the form of a 20-acre tract of land known as the South One-half (½) of the North [fol. 14] One-half (½), and the North One-half (½) of the South One-half (½) of Lot One (1), Block Twenty-three (23) of the Rio Grande Development Company's Subdivision of Lands, Hidalgo County, Texas, agreeing to pay therefor the sum of $8,000.00, paying $4,000.00 in cash down, and executing five notes in the sum of $800.00 each due annually thereafter bearing interest at the rate of five (5) per cent per annum, and further paying the sum of $2,500.00 in cash for said citrus trees. That since said

purchase, the Plaintiff has paid the sum of $1,593.08 for care for said trees, $14.73 for taxes, and $1,100.00 on Note No. 1, plus accrued interest, and an additional $200.00 in investigating the investment and discovering the true facts concerning said investment. That said purchase contract was executed by Carl Pummill as President of Pummill Development Company, and the Plaintiff, W. H. Ham, and a warranty deed to said property was subsequently issued to Plaintiff dated March 3, 1950, and now of record in the Deed Records of Hidalgo County, Texas, in Vol. 703, pages 155-157. That on the 1st day of April, 1950, the Pummill Management Company executed and delivered to the said Plaintiff a care contract by which they agreed to care for the property for five years, with the Plaintiff to continue to invest money in said property through such care, by depositing sufficient sums from time to time in the First National Bank of Mission, Texas, to the joint account of the Plaintiff and Pummill Management Company. Such in-[fol. 15] vestment was to continue during the five-year period of the contract. The aforesaid deeds and care contracts, as well as monthly statements on the investment to be made in the care, were forwarded to the Plaintiff through the United States Mails. That to the date of this suit, Plaintiff has invested in said security the sum of $9,407.81, and has had no return of any kind since the purchase of said security and/or investment contract.

(8) That pursuant to said plan and scheme, the Plaintiff Herbert Clark did, on March 3, 1950, purchase said security and/or investment contract in the form of a 20-acre tract of land known as the South One-half (½) of the South One-half (½) of Lot One (1), Block Twenty-three (23), and the North One-half (½) of the North One-half (½) of the West One-half (½) of Lot Six (6), Block Twenty-three (23), Rio Grande Development Company's Subdivision of Lands, Hidalgo County, Texas, agreeing to pay therefor the sum of $8,000.00, which was then paid in cash, and further paying the sum of $2,500.00 in cash for said citrus trees. That since said purchase, the Plaintiff has spent the sum of $1,585.04 for care for said trees, $14.73 for taxes, and an additional $200.00 in investigating the investment and discovering the true facts concerning said investment. That said purchase contract was executed by Carl Pummill as

President of Pummill Development Company, and the Plaintiff, Herbert Clark, and a warranty deed to said property [fol. 16] was subsequently issued to Plaintiff dated March 3, 1950, and now of record in Vol. 701, page 540-42 of the Deed Records of Hidalgo County, Texas. That on the 1st day of April, 1950, the Pummill Management Company executed and delivered to the said Plaintiff a care contract by which they agreed to care for the property for five years, with the Plaintiff to continue to invest money in said property through such care, by depositing sufficient sums from time to time in the First National Bank of Mission, Texas, to the joint account of the Plaintiff and Pummill Management Company. Such investment was to continue during the five-year period of the contract. The aforesaid deed and care contract, as well as monthly statements on the investment to be made in care, were forwarded to the Plaintiff through the United States Mails. That to the date of this suit, Plaintiff has invested in said security the sum of $12,299.77, and has had no return of any kind since the purchase of said security and/or investment contract.

IV

Plaintiffs were induced to sign said investment contract and/or purchase such securities because of their reliance upon fraudulent inducements and false representations of material, existing facts, or fraudulent concealment thereof, which representations and Plaintiffs' reliance thereon were the result of the cumulative effect of the wrongful acts of each and all Defendants in conspiracy, each Defendant performing some indispensable part of the whole plan, which [fol. 17] was designed to and did result in the plundering of Plaintiffs. The representations which were made were as follows, to wit:

1. That by investing in said Citrus Development at this time, Plaintiffs could get in on an 800-acre unit which would be developed by one company in a uniform manner and under the management of citrus experts, for the joint benefit of all investors.

2. That at the end of three years, the property would be paying all of its own expenses.

3. That said investment would produce a minimum of a 20% per year return on the money invested, after five years.

4. That said property was in Water District No. 7, and that while no canals were available on the property at the present time, they would be extended within a maximum of one and one-half years, and that the citrus trees planted before then would be tank watered with water from said district, so there was no reason for delay in planting said trees.

5. That said land was some of the best citrus land in the Rio Grande Valley, and was being sold at the pre-war price of $400.00 per acre, and if not bought now, would not be available at that price.

6. That the land was worth more than $400.00 per acre, and land equally as good could not be bought for that price [fol. 18] anywhere in the Rio Grande Valley.

7. That only the finest citrus stock in the Rio Grande Valley would be used in the planting of said property.

8. That the investor would not have a thing to worry about. The Pummill Management Company would take care of all of the problems which might arise, and the investor would only have to sit back and reap the dividends.

9. That the reason the investor was only getting one-eighth of the customary one-eighth mineral interest was because this was the only interest Pummill Development Company had in said minerals.

10. That good irrigation water was being put on the young citrus trees since bills for water were sent to the Plaintiffs each month prior to their additional investments in care for said trees.

V

That had the representations in Paragraph IV not been made to the Plaintiffs, they would not have made said investment. That said representations were made to the Plaintiffs for the express purpose of inducing Plaintiffs to purchase, that said representations were known to be false and fraudulent by the Defendants at the time they were made, that said representations were of material facts and were false at the time they were made, and the Plaintiffs were damaged by receiving worthless property. That after said oral false and fraudulent representations were

[fol. 19] made to the Plaintiffs, the Defendants forwarded the deeds, contracts and statements to the Plaintiffs through the United States Mails, and continued to make false representations by sending to Plaintiffs, through the United States Mails, various care bills including therein charges for irrigation water which was neither used nor available to the Defendants for such use.

VI

That sometime during the months of February, March and April, 1951, the Plaintiffs jointly discovered that the representations set forth in Paragraph IV were false and fraudulent, and that the true facts concerning their investment were as follows:

1. That Pummill Management Company was not developing said 800 acres in a uniform manner, but was in fact subletting the care to other people, who were neglecting said property. That Pummill Management Company were not experts in the care of citrus, and did not have the necessary equipment to care for the property.

2. That the property was not developing at all, but on the contrary, the trees which were planted were not growing, and a great many of them were dead. That under no circumstances would the property be paying for itself within five years.

3. That said property was not capable of being developed [fol. 20] into bearing citrus groves, and would never pay any return on the investment.

4. That said property was being taken out of Water District No. 7, and that the canals of said district could not be extended to this land, because there was inadequate water from the Rio Grande available for the land in District No. 7 already equipped with canals. Further, that the Defendants could not get suitable water for the irrigation of said trees, but in fact used refuse drain ditch salt water on said trees, which caused most of them to die.

5. That said land was not in fact citrus land, and instead of being worth $400.00 per acre, was only worth about $50.00 per acre as dry farm land.

6. That the citrus stock used for planting said land was

of an inferior quality and would produce only diseased and stunted trees.

7. That Pummill Management Company ceased to care for the property on January 31, 1951, and prior to that time had neglected the property and failed to care for it in a prudent manner.

8. That Pummill Development Company in fact owned twice as much of the minerals in and under said land as it conveyed to the Plaintiffs.

9. That the water used by Pummill Management Company on said trees was refuse drainage ditch salt water [fol. 21] which cost nothing, but that said company had been billing the Plaintiffs for good irrigation water.

That by virtue of the misrepresentations made by the Defendants in the sale of the investment contract and/or security to the Plaintiffs, said Defendants have violated the provisions of Section 77 1. (2) of the Securities Act of 1933 and Section 77 q. of said act, and are jointly and severally liable to the Plaintiffs for return of the money and property expended in their investment, and the Plaintiffs here tender back to the Defendants the investment contracts or securities purchased, together with the land which they now hold under said investment contracts.

VII

Each of the Defendant took part in the sale of said securities and/or investment contracts, either directly or as co-conspirators, agents, employees or by agreement.

1. Lloyd M. Bentsen, Sr., and Elmer C. Bentsen, acting individually and through Bentsen Development Company, a partnership, made available to the other defendants an 800-acre tract of land, which constituted the subject matter of the investment contracts sold under the plan and scheme; such land, with the minerals, would have had an actual value of $40,000.00, but said Lloyd M. and Elmer C. Bentsen reserved the minerals to themselves, thereby reducing the actual value of the land to a figure considerably under $40,000.00, and through the fraudulent artifice of a simulated vendor's lien, over $100,000.00 in excess of such [fol. 22] value, retained both their control over the land and the over-all operations of all defendants under the plan and scheme, while at the same time protecting and securing their interest in the division of the spoils and

plunder to be taken under the scheme; they looked, not to the insolvent Pummill Development Company for payment of said excess and fraudulent value thus impregnated into the whole scheme, but rather to the members of the buying public, to be procured through the activities and efforts of other defendants; they received additional benefits by selling at current prices for good citrus nursery stock cull citrus stock to be planted on said land, and exerted additional control through advancing the funds required for the operation of said selling and care companies.

2. G. F. Dohrn was attorney for the organization of Pummill Development Company and was instrumental as a go between for Lloyd M. Bentsen, Sr., Elmer C. Bentsen and the Pummill Corporations and the other Defendants, and assisted the Bentsens in controlling the operation.

3. Earl Pummill and Carl Pummill were the organizers of Pummill Development Company and the Pummill Management Company, Directors and Stockholders, and each directly made the representations set out in Paragraph IV above.

4. Albert L. Richter is Secretary of Pummill Management Company and as such officer was directly responsible for the continuing misrepresentations concerning care bills [fol. 23] for the property, and was instrumental in keeping the Plaintiffs from discovering the true facts concerning their investment.

5. R. B. Kale, representing himself as a broker, showed the property to Paul Boyd, of Boyd Construction Company, and directly assisted other Defendants in selling said investment contract to the Plaintiff, Boyd Construction Company. He received a commission from the other Defendants for his part in the sale to this Plaintiff.

6. C. W. Norton, as a driver of a sight-seeing tour for Pummill Development Company, made many of the false and fraudulent representations to the Plaintiffs, and was active in inducing the Plaintiffs to purchase said securities and/or investment contracts.

7. C. A. Conner, representing himself as a broker, showed the property to Clyde W. Weatherly and directly assisted other Defendants in selling said investment contract to the Plaintiff, Clyde W. Weatherly, and received a commission therefor.

8. O. M. Ohmit induced the Plaintiffs, Arie K. Smith, Dudley Smith, W. H. Ham and Herbert Clark to make a trip to the Rio Grande Valley, representing himself as a broker for the Pummill Development Company, and assisted the other Defendants in selling said investment contract to these Plaintiffs. He received a commission from the other Defendants for his part in the sale to these Plaintiffs.

9. Allen Beckham, representing himself as a broker, [fol. 24] showed the property to Emery C. Blackwell, and directly assisted other Defendants in selling said investment contract to the Plaintiff Emery C. Blackwell, and received a commission therefor.

All of the Defendants herein are jointly and severally liable to these Plaintiffs for their part in the general plan and scheme, as principals, agents, employees, co-conspirators, or as a result of written or oral agreements between themselves, both as a result of their violation of the Securities Act of 1933 and under the Statutes of the State of Texas, and the Plaintiffs are entitled to return of their purchase money, expended on said securities and/or investment contracts, and in addition thereto are entitled to exemplary damages as a result of the false and fraudulent representations in double the amount of actual damages.

The Plaintiffs would further show the Court that they have agreed to pay the undersigned attorneys the sum of $4,000.00 for bringing this suit, which is a reasonable amount therefor, and an additional sum in the event recovery is had in said suit, such sum to be determined by the final recovery had in said suit.

Wherefore, premises considered, Plaintiffs pray that the Defendants be cited to appear and answer herein, and that on final hearing, Plaintiffs have judgment against each and every Defendant, jointly and severally, for the cancellation [fol. 25] and rescission of said investment contract and/or security purchase, cancellation of the Deeds and Vendor's Lien Notes owed by the Plaintiffs, and for return of all of the money expended in the purchase of said securities and/or investment contracts, in the total sum of $92,137.46, plus exemplary damages in double that amount, for their costs herein expended, for interest on said sums, for reasonable attorney's fees as may be decided upon by the Court,

and for such other and further relief as they may be entitled to receive, either at law or in equity.

That in the alternative, in the event that the Court, on final hearing, should deny the Plaintiffs the remedy of cancellation and rescission based on violations of the Securities Act of 1933, then the Plaintiffs pray for cancellation and rescission of said transaction and return of the monies expended under the laws of the State of Texas, plus interest, costs, attorney's fees, exemplary damages in double the amount of actual damages, and such other and further relief as they may be entitled to receive, either at law or in equity.

That in the alternative, in the event that the Court, on final hearing, should deny the Plaintiffs the remedy of cancellation and rescission, that they be given damages in the sum of $350.00 per acre, being the difference between the value of the land as actually delivered, and the price paid therefor, plus all sums expended for trees and care, and an additional recovery of double that amount as exemplary damages as authorized by Article 4004, Revised [fol. 26] Civil Statutes of Texas, 1925, in the total sum of $353,332.38, plus interest, costs, and attorney's fees, together with such other and further relief as they may be entitled to receive at law or in equity.

Respectfully submitted, Smith, McIlheran & Smith.
By: (S.) E. H. McIlheran, Attorneys for Plaintiffs, Weslaco, Texas.

In United States District Court

Consolidated Motions of Defendants Lloyd M. Bentsen, Sr., et al.—Filed September 7, 1951

To the Honorable Court:

Come now Lloyd M. Bentsen, Sr., Elmer C. Bentsen, and Bentsen Development Company, Defendants in the above entitled and numbered cause, and in response to summons thereon file their Consolidated Motions to dismiss, to strike, and for a more definite statement, pursuant to Rule 12 of

the Federal Rules of Civil Procedure, and respectfully move the Court in the following particulars:

[fol. 27] I. *Motion to Dismiss for Lack of Jurisdiction:*

These Defendants move this Honorable Court to dismiss the Plaintiffs' action as to them because the Court does not have jurisdiction of the subject matter of such action and should take no further cognizance of it other than to dismiss it as to these Defendants, and more specifically, would show to the Court:

(a) The Plaintiffs' petition or complaint alleges that the action arises under the Securities Act of 1933, May 27, 1933, c. 38 Title I, #48 Stat. 74 and more particularly under Sections 77 1.(2) and 77 q. of the said Securities Act of 1933 (Paragraphs I and II of the Plaintiffs' petition) Title 15 U. S. C. A. Section 77 1.(2) and 77 q.; but the complaint does not contain sufficient factual allegations to present a substantial question under the provisions of the cited sections of the Act upon which the Plaintiffs rely. These Defendants submit that if the allegations that certain deeds or monthly statements were forwarded to the Plaintiffs through the United States mails were true (of which these Defendants have no knowledge) the same are not sufficient to constitute an allegation of jurisdictional facts under the cited sections of the Act or to present a Federal question thereunder, in that it is nowhere alleged that such deeds or statements constituted a prospectus or a communication in the sale of securities nor that they were a representation in the sale of the land involved nor that they were made or forwarded through the mails for the purpose of inducing the Plaintiffs to purchase the property. [fol. 28] These Defendants respectfully submit that not only the provisions of said Sections 77 1.(2) and 77 q. but the intendment of the Securities Act of 1933 as a whole, are directed to the regulation of the sale of securities through the mails or in Interstate Commerce and that the gravamen of any action thereunder is that there has been misrepresentation on the part of the Defendants or misleading of the Plaintiffs through the means of instruments specified in the Act and that an allegation of the forwarding of a deed or monthly statement without alleging wherein they were representations or were misleading, is insufficient to

present a Federal question under the Act; and further, that the Plaintiffs' cause of action, if any they have, is simply one for cancellation and recission and that the allegations of it arising under the Securities Act or that certain deeds and statements were forwarded through the mails are calculated to impose upon the jurisdiction of this Honorable Court through broad, general and indefinite conclusions without alleging the necessary jurisdictional facts.

(b) These Defendants submit that this Honorable Court does not have jurisdiction of the Plaintiffs' actions in so far as these Defendants are concerned, regardless of the merits of the action as to the other Defendants. In this connection, these Defendants submit that the Plaintiffs' complaint improperly and prejudicially includes these Defendants with all of the others without making any specific factual allegations to support the Court's jurisdiction under [fol. 29] the Securities Act of the Plaintiffs' action as to these Defendants. The complaint or petition includes vague, indefinite, prejudicial and argumentative allegations which are nowhere explained or supported by specific allegations showing in any way these Defendants' connection with the transactions forming the basis of the Plaintiffs' action or that the facts upon which the Plaintiffs rely to support the jurisdiction of this Court; and if the allegations as to the use of the mails were sufficient to support the Court's jurisdiction as to the other Defendants, the complaint is insufficient to show any connection with the transactions of these Defendants under general rules of pleading as well as under Rule 9(b) of Federal Rules of Civil Procedure.

(c) Further, and in the alternative (as plead in the Plaintiffs' complaint) this Court does not have jurisdiction to hear and determine the Plaintiffs' action for the alternative relief sought in the prayer (pages 16 and 17). It has been submitted hereinabove that the Plaintiffs' allegations of their action arising under the Securities Act do not present a substantial Federal question in support of the jurisdiction of this Court and that their allegations pertaining to the said Act and the use of the mails are calculated to impose upon the jurisdiction of the Court. In the prayer of the Plaintiffs' petition alternative relief

under the laws of the State of Texas is sought and these Defendants submit that this Court does not have juris-
[fol. 30] diction to hear and determine the Plaintiffs' action in connection with such alternative relief. The alternative relief of the said prayer of the petition is the subject of a non-Federal cause of action separate and distinct from that attempted to be brought under the cited provisions of the Securities Act and, regardless of this Court's jurisdiction of the Plaintiffs' action under the Federal statute vel non, it does not have the authority to hear and determine the matters of the alternative relief in that either the lack of jurisdiction or the denial of relief on the basis of the Federal Statute would preclude its hearing or granting alternative relief in the non-federal causes.

II. *Motion to Dismiss for Failure to State a Claim Upon Which Relief Can Be Granted:*

Subject to the Court's ruling on the foregoing Motion to Dismiss for Lack of Jurisdiction, these Defendants now move the Court to dismiss the Plaintiffs' action as to them because the complaint fails to state a claim or claims upon which relief against these Defendants could be granted to the Plaintiffs. In this connection, these Defendants submit that in paragraph VII of the complaint the Plaintiffs have sought to join these Defendants through the use of vague, indefinite and argumentative allegations without alleging any specific facts as to these Defendants' connection with the transactions complained of; and the Plaintiffs have alleged that the Defendants' action is in the nature of a conspiracy to defraud members of the buying public with-
[fol. 31] out showing definitely and certainly any connection of these Defendants with the transactions complained of. These Defendants submit that the allegations through which the Plaintiffs seek to join them in the cause of action are mere conclusions unsupported by any factual allegations and are wholly insufficient to state a claim upon which relief against these Defendants could be granted to the Plaintiffs by this Honorable Court.

III. *Motion to Dismiss the Plaintiffs' Class Action:*

Subject to the foregoing motion these Defendants move this Honorable Court to dismiss the Plaintiffs' action as a class action and would show as reasons therefor that the allegations pertaining to this type of action through which the Plaintiffs purport to act for others not parties to the suit on the basis of virtual representation are entirely insufficient to support such an action. In this connection, it is submitted that the Plaintiffs do not allege that it would be impractical to bring all parties similarly situated before the Court; that all such parties are similarly affected in respect to the matters of the suit; nor that the suit is of such a nature that other persons having similar transactions are dissatisfied with their purchases and would desire to complain in the matters of the Plaintiffs' suit. Further, the allegation that there are common questions of law and fact involved is a mere conclusion unsupported by sufficient [fol. 32] allegations and in this connection these Defendants would show that the very nature of the transactions alleged in paragraph III of the complaint made it manifest that distinguishable questions both of law and of fact would probably arise.

IV. *Motion to Dismiss for Misjoinder of Parties:*

Subject to the foregoing, these Defendants now move this Honorable Court to dismiss the Plaintiffs' action because of misjoinder of parties both Plaintiffs and Defendants. The Plaintiffs' complaint makes it manifest that they have been improperly joined in their action against the several Defendants in that each of the transactions alleged in paragraph III of the complaint are matters of individual contracts with the Defendants other than these to each of which the Defendants are entitled to prepare separate defenses, and the joining of which results in the considerable complexities in the trial of the claims and requires the Defendants in effect to meet and defend eight separate actions simultaneously. The joinder of the Defendants in this action is unduly prejudicial and burdensome and the Plaintiffs' actions, if any they have, are separate causes of action based upon the respective contracts and facts in

each case. These Defendants further submit that there has been an improper joinder of Defendants in the Plaintiffs' action in that while the Plaintiffs have named these Defendants in their complaint they have not made allegations sufficient to justify their joinder with the other De-
[fol. 33] fendants; and in this connection the Defendants would show that they have been joined solely on the basis of vague, indefinite and argumentative pleadings but that nowhere are there any specific facts alleged as to these Defendants' connection with the transactions or participation in the alleged conspiracy, and the same is expressly required by Rule 9(b) of the Federal Rules of Civil Procedure.

V. *Motion to Direct Plaintiffs to Amend and File a More Definite Statement*

Subject to the foregoing, these Defendants now move the Court that the Plaintiffs be directed to amend their complaint severing their several causes of action in separate counts in respect to the claims of each of the Plaintiffs and to require the Plaintiffs to file a more definite statement or a Bill of Particulars, setting forth with definiteness and certainty jurisdictional facts and the facts on which they seek to hold these Defendants in their action and, more specifically, these Defendants desire a more definite statement as to the following matters:

(a) The connection of these Defendants with the alleged conspiracy and fraud, the part that the Plaintiffs claim they took in it, and their connection with transactions between the other Defendants and the several Plaintiffs.

(b) The contents of the deeds, contracts, and monthly statements referred to in the complaint and the matters [fol. 34] thereof that constituted a misrepresentation in the sale under the Securities Act of 1933.

(c) The specific deeds, contracts and monthly statements between the Plaintiffs and other Defendants herein, giving the parties, the dates and the facts attending the execution of each.

(d) The connection of these Defendants with the other Defendants (Pummill Development Company) and the specific facts on the basis of which the complaint alleges that

these Defendants had some control over the action of the other Defendants.

(e) The names of the several Defendants who made each and all of the representations alleged in paragraph IV and the places, time and manner in which the representations were made.

(f) The specific manner in which these Defendants "made available to other Defendants" an 800 acre tract of land.

(g) The specific means or manner in which these Defendants "retained both their control over the land and the over-all operations" of the other Defendants.

(h) The specific means or manner through which these Defendants had an interest in "the spoils and plunder to be taken under the scheme".

(i) The specific facts and circumstances constituting the "fraudulent artifice of a simulated vendor's lien".

[fol. 35] (j) The benefits derived by these Defendants (as implied in the complaint) from the transactions between the several Plaintiffs and the other Defendants, and the manner and the time and the nature of such benefits.

(k) The specific circumstances constituting the alleged plan or scheme and facts to support the Plaintiffs' allegation that these Defendants participated in the same.

These Defendants submit that Rule 9(b) of Federal Rules of Civil Procedure requires particularity in all allegations of fraud or conspiracy to defraud and that these Defendants are entitled to have the Plaintiffs plead specific factual allegations as to their joinder in the suit.

Wherefore, these Defendants pray that the Court consider the foregoing motions in the order presented and that said motions be sustained, and that these Defendants go hence with their costs without day.

Kelly, Looney, McLean & Littleton. By (s) Jackson Littleton, Attorneys for Defendants, Lloyd M. Bentsen, Sr., and Elmer C. Bentsen and Bentsen Development Company.

Certificate of service (omitted in printing).

[fol. 36] IN UNITED STATES DISTRICT COURT

CONSOLIDATED MOTIONS OF DEFENDANTS EARL PUMMILL, ET AL.—Filed September 1, 1951

The defendants Earl Pummill, Carl Pummill, Albert L. Richter, C. W. Norton, L. H. Ramey, Pummill Development Company and Pummill Management Company move the Court as follows:

1. To dismiss the action on the ground that the Court lacks jurisdiction because it affirmatively appears from plaintiffs' complaint that no Federal question is involved in that the acts complained of did not involve the sale of any security under the Securities Act of 1933.

2. To dismiss the action as a class action because the complaint fails to state a claim or claims properly brought against these defendants as a class action and the complaint should be stricken insofar as it purports to be a representative action.

3. To dismiss the action because the complaint fails to state a claim or claims in behalf of any of the plaintiffs against any of these defendants upon which relief can be granted and more particularly in that:

a. No facts sufficient at law to support a claim under the Securities Act of 1933 are alleged as against any of these [fol. 37] defendants, and

b. No facts sufficient to support actionable fraud at common law are alleged as against any of these defendants, and

c. No facts sufficient to support an action for damages under the Statutes of the State of Texas are alleged as against any of these defendants.

4. To dismiss the action because the complaint has a misjoinder of parties plaintiff and claims because by combining unrelated claims and parties it will make it impossible for these defendants to prepare separate defenses to the commingled claims asserted and will make trial of individual claims unwieldy and prejudical to these defendants.

5. To direct plaintiffs to serve an amended complaint herein stating in separate counts any claims based on the

Securities Act of 1933, the common law and the statutes of Texas and the claims of the various plaintiffs on the ground that each of the plaintiffs' claims are founded on separate transactions and separate statement is essential to the clear presentation of the matters set forth and for the further reason that each plaintiff is endeavoring to assert in a single count three separate and distinct claims.

6. To direct the plaintiffs to file a more definite statement or a bill of particulars of the following matters:

a. The representations or concealments with which each of them is charged by each of the plaintiffs, and

b. The written or oral agreements which plaintiffs allege [fol. 38] on page 15 of the complaint that all defendants had between themselves.

The above matters are not averred with sufficient definiteness or particularity to enable any of these defendants to properly prepare their answers. The glittering generalities and general charges on the part of these plaintiffs in this regard do not comply with Rule 9(b) as to particularity. This is particularly true of defendants Norton, Richter and Ramey.

Respectfully, Hill, Lochridge and King, by (S) Lloyd Lochridge, a member of the Firm; Attorneys for Earl Pummill, Carl Pummill, Albert L. Richter, C. W. Norton, L. H. Ramey, Pummill Development Company and Pummill Management Company, Saxet Building, P. O. Box 32, Mission, Texas.

In United States District Court

Motion of R. B. Kale—Filed September 13, 1951

The defendant R. B. Kale moves the court as follows:

1. This defendant here and now adopts and incorporates by reference herein the consolidated motion of defendants Earl Pummill, Carl Pummill, Albert L. Richter, C. W. Nor- [fol. 39] ton, L. H. Ramey, Pummill Development Company

and Pummill Management Company on file herein and urges the court as said defendants do in said motion.

Respectfully, Hill, Lochridge and King, Box 32, Mission, Texas; by (s) Lloyd P. Lochridge, Jr., a member of the firm, Attorneys for R. B. Kale.

Certificate of service (omitted in printing).

IN UNITED STATES DISTRICT COURT

MOTION OF G. F. DOHRN—Filed September 19, 1951

Comes now G. F. Dohrn, Defendant in the above entitled and numbered cause, and in response to summons therein files this his Consolidated Motions to dismiss, to strike, and for a more definite statement pursuant to Rule 12 of Federal Rules of Civil Procedure; and in connection with such mo-
[fol. 40] tions would respectfully show to the Court that this Defendant adopts each and all of the motions heretofore filed on behalf of the Defendants, Lloyd M. Bentsen, Sr., and Elmer C. Bentsen, and joins in all of the matters set forth for the Court's consideration in the several motions so filed.

Wherefore, this Defendant prays that the Court consider the several motions filed on behalf of the said Defendants as having been also presented by this Defendant; that each of the said motions be considered in the order presented and that they be in all things sustained and that this Defendant go hence with his costs without day.

(s) G. F. Dohrn.

Certificate of service (omitted in printing).

IN UNITED STATES DISTRICT COURT

MOTION OF FRANK L. DANNER TO INTERVENE—Filed December 29, 1951

Frank L. Danner moves for leave to intervene as a Plaintiff in this action, in order to assert the claim set forth in his proposed complaint, of which a copy is hereto attached, [fol. 41] on the ground that he is a member of the class constituting the Plaintiffs in said action, or if the Court should find that the complaint does not state a true class action, then that he is entitled to join the other Plaintiffs under the permissive joinder rules, since this Applicant purchased his security and/or investment contract under the same false and fraudulent representations in violation of the Security Act of 1933, May 27, 1933, c. 38, Title I, #48 Stat. 74, as more fully set out in the proposed complaint, and this Applicant's claim presents both questions of law and fact which are common to the main action.

Smith, McIlheran & Smith, by: (S) E. H. McIlheran, Attorneys for Frank L. Danner, 516 Texas Blvd., Weslaco, Texas.

To: Hill, Lochridge & King, Attorneys at Law, Mission, Texas; Kelley, Looney, McLean & Littleton, Attorneys at Law, Edinburg, Texas; Attorneys of Record for the Defendants

Please take notice that the undersigned will bring the above motion on for hearing before this Court at the United States Courts and Post Office Building, Corpus Christi, [fol. 42] Texas, on the 14th day of January, 1952, at 10:00 o'clock in the forenoon of that day or as soon thereafter as counsel can be heard.

Smith, McIlheran & Smith, by: (s) E. H. McIlheran, Attorneys for Frank L. Danner, 516 Texas Blvd., Weslaco, Texas.

We hereby certify that on the 28th day of December, 1951, we served copies of the foregoing Motion and attached Complaint in Intervention upon Hill, Lochridge & King and Kelley, Looney, McLean & Littleton, Attorneys for the Defendants, by depositing said copies in the United States

Mails, postage prepaid, in envelopes addressed respectively to each of said Attorneys at their respective addresses as set out in the foregoing notice, which addresses are the last addresses of the Attorneys known to us.

Smith, McIlheran & Smith, By: (s) E. H. McIlheran, Attorneys for Frank L. Danner, 516 Texas Blvd., Weslaco, Texas.

COMPLAINT IN INTERVENTION

To the Honorable James V. Allred, Judge of Said Court:

Frank L. Danner, an individual resident of Tarrant County, Texas, for his complaint in intervention as a party plaintiff alleges:

I

That on January 24, 1950, intervening plaintiff, Frank L. [fol. 43] Danner purchased a security and/or investment contract in the form of a 40-acre tract of land planted to young citrus trees known as the West one-half (½) of Lot Number Seven (7), Block Number Twenty-six (26), Rio Grande Development Company's Subdivision, Hidalgo County, Texas, under the same false and fraudulent representations set out in said original complaint, paying therefor the sum of $16,000.00 cash, further paying the sum of $5,000.00 to have said land planted to young citrus trees, and subsequent to that date he expended the total sum of $1,155.00 on the care of said trees and/or investment contract, and an additional sum of $200.00 in finding out the true facts concerning his investment.

II

That said intervening planitiff, prior to finding out the true facts concerning his purchase, did on February 21, 1951, sell said security and/or investment contract to Lloyd M. Bentsen, Sr., one of the Defendants, for the sum of $7,000.00, thereby sustaining a loss of $14,355.00.

III

That the above described purchase was evidenced by a contract with Pummill Development Company, executed by

Carl Pummill and dated January 24, 1950, and the above described care payments were made pursuant to a care contract with Pummill Management Company dated February 15, 1950, but executed on January 24, 1950. The pur-
[fol. 44] chase was evidenced by a Warranty Deed from Pummill Development Company dated January 24, 1950 and recorded on March 20, 1950 in Vol. 684, page 188 of the Deed Records of Hidalgo County, Texas.

IV

Intervening plaintiff adopts all of the allegations of the original complaint filed in this suit;

Wherefore, premises considered, intervening plaintiff prays for leave to intervene, and that on final hearing he have the relief allowed under the Securities Act of 1933, or the alternative relief prayed for in said Original Complaint.

Smith, McIlheran & Smith, By: (s) E. H. McIlheran,
Attorneys for Frank L. Danner, 516 Texas, Blvd.,
Weslaco, Texas.

In United States District Court

Order Granting Leave to Intervene—Entered March 21, 1952

3-21-52—Leave to intervene granted.

Clerk notify counsel.

JVA.

[fol. 45] In United States District Court

Affidavit Attached to Brief—Filed October 15, 1951

State of Texas,
County of Hidalgo:

Before me, the undersigned authority, on this day personally appeared Carl Pummill and who, being duly sworn does depose and say:

1. My name is Carl Pummill. I am President of the Pummill Management Company, a defendant in Civil

Cause No. 728 styled Emery C. Blackwell et al. v. Lloyd M. Bentsen, Sr., et al., pending in the United States District Court for the Southern District of Texas, Brownsville Division. This affidavit is made with reference to the motion to the jurisdiction pending in this suit.

2. Each of the plaintiffs Claude E. Blackwell, Clyde W. Weatherly, Arie K. Smith, Dudley Smith, W. H. Ham and Herbert Clark entered into a management contract with Pummill Management Company covering lands described in plaintiffs' complaint on file herein. Paul J. Boyd Construction Company, a Minnesota corporation, entered into a management contract with Pummill Management Company on February 24, 1950. No management contract was entered into with the plaintiff Boyd Construction Company, a Texas corporation. Each such management contract was on a mimeographed form reading as follows:

[fol. 46] Management Contract

STATE OF TEXAS,
County of ——:

The following contract is hereby made and entered into this — day of ——, 1950, by and between ———— ———— of —— County, —— (hereinafter known as First Party) and Pummill Management Company, a corporation, of Mission, Texas (Hereinafter known as Second Party).

Witnesseth:

First Party is the owner of:

containing — acres of grove, more or less, and hereby contracts with the Second Party to supervise the care of the grove located on said premises for a period of not less than one (1) year from the date hereof and to continue thereafter on an annual basis from year to year for a period of five (5) years. However, First Party may terminate this contract by giving written notice to that effect by registered mail at any time during the life of this contract and upon receipt of such notice by Second Party, the contract will terminate thirty (30) days after the mailing of such notice. Second Party may terminate this contract by giving written notice to that effect by registered mail during the month of

January of any year during the life of this contract and upon the mailing of such notice, the contract will terminate [fol. 47] on the first day of February after the mailing of such notice. It is understood, however, that First Party shall not have the right to terminate this contract unless all amounts due Second Party hereunder are paid in full to the date of such termination.

It is hereby agreed that as compensation for the management of the care of said grove, Second Party shall receive One Dollar ($1.00) per acre per month payable in advance, at Mission, Texas. In addition to the above, First Party shall pay promptly as used, the cost of any and all labor and materials used in the normal care of the grove on the basis of the prevailing local charge for doing such work, the cost of all water used in irrigation, the cost of all materials used in dusting and fertilizing and the cost of seed for cover crops and shall pay a reasonable charge for the application of such materials and planting of such cover crop. It is agreed, however, that fertilizer and cover crop will not be used except as directed by owner.

It is agreed that First Party shall pay all these above mentioned costs through the establishment of a fund in the amount of —— Dollars ($—) at —— Bank of ——, Texas. Second Party shall have the authority to write checks on such account for the payment of all work done and all materials used in the care of the grove, and for compensation for supervision due it as herein provided. At the end of each [fol. 48] month, Second Party shall send to First Party a complete accounting of all amounts expended in the care of the grove. Upon receipt of such accounting, First Party shall, within ten (10) days, replenish the said bank account in full to the amount of the original deposit. This deposit shall be withdrawable by First Party ten (10) days after written notice to Second Party that such withdrawal is going to be made.

Since it is necessary that all work in the grove be done when and as needed for the protection of the grove, it is hereby agreed that if First Party shall, at any time during the life of this contract, fail to make such deposits within thirty (30) days of the aforementioned accounting, that such failure will release Second Party from any liability or responsibility to either fruit or grove by not having such

work done when and as needed. It is further agreed that if such default should occur that Second Party shall have the right to cancel and nullify this contract. It is understood that should this contract be nullified in the above mentioned manner that First Party shall be liable for all accrued bills, contract in the working of his land up to and including the termination date of the contract as herein specified.

The term "care" as used herein obligates Second Party to cause to be done all things pertaining to the care of the grove which Second Party believes to be necessary and to the best interest of the grove and of First Party, including [fol. 49] all cultivation of the grove, banking and removing of banks from trees three years old or less when banking is normally deemed avisable, irrigation, dusting, fertilizing, cover crop planting, etc. Second Party is to use his own best judgment as to when and to what extent the above work is to be performed, and shall, in addition, cause any other care work to be performed which the owner may request. Should major pruning be necessary, it will be done when ordered by owner and at an agreed price.

Second Party shall be liable to First Party, his executors, administrators, successors and assigns for any loss, injury or damage sustained on account of his acts or omissions, or that of his agents, amounting to negligence. Second Party does not assume responsibility for loss, injury or damage sustained by fire or any other cause resulting from the negligence of any person other than himself or his agents, nor for storm, wind, extremes of temperature and other acts of God, nor from strikes or other acts of the Public Enemy, lockouts, shortage of labor, fuel, water or materials. Second Party does not assume responsiblity for any material increase in the cost of labor, fuel, materials, or supplies, or any Governmental tax, supervision, regulation, legislation, or any cause beyond the control of Second Party. Any necessary change in either care or charges shall be made after mutual agreement.

It is hereby agreed that it shall be the responsibility of Second Party to see to the harvesting and marketing of all [fol. 50] fruit produced on the above described lands during the life of this contract. Second Party shall use all dili-

gence in such marketing and harvesting and shall see that all crops are removed and processed in due time and season to the best of his judgment and ability. However, First Party shall notify Second Party in writing prior to the marketing of all fruit crops as to the manner in which First Party prefers and directs that such crops shall be marketed and/or whether First Party has entered into any sale marketing agreement or association agreement with a third party or parties for the harvesting, marketing and sale of such crops. Should First Party enter into any such contract or agreement as above mentioned, Second Party shall give full cooperation to such third party in order that all crops may be harvested and marketed to the best advantage and shall, in addition, check and keep a complete accounting of such harvesting and marketing. Second Party shall collect and keep full accounting of all amounts due First Party from fruits and/or crops and shall remit same to First Party at the end of the harvesting season or shall remit any amounts collected during the season if so directed by First Party.

In consideration for the above described services, Second Party shall be entitled to and shall deduct from and retain five (5) per cent from all remittances due First Party at the time such remittance is made to First Party.

All amounts which may become due by First Party to [fol. 51] Second Party in this contract provided for, if not paid when due, shall thereafter bear interest at the rate of six per cent (6%) per annum until paid, and if by reason of default in payment Second Party places the same in the hands of an attorney for collection, First Party will pay an additional amount of ten per cent (10%) on the amount so in default as attorneys fees for collection, and the payment of all such amounts, including interest and attorneys fees, shall be, and is hereby secured by a lien on the land above described, and all net proceeds of the sale thereof or any crops growing or to be grown thereon, and an executed copy of this contract may be filed and registered in the Chattel Mortgage Records of said —— County as a Chattel Mortgage on the fruit crop.

Witness the hands of the parties hereto the day and year first above written.

—— ——, First Party; Pummill Management Company, by —— ——, President.

Attest: —— ——, Secretary.

The State of ————,
County of ————:

Before me, the undersigned, a Notary Public in and for said County and State, on this day personally appeared [fol. 52] —— ——, known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this the -- day of ——, A. D. 195—.

—— ——, Notary Public in and for —— County, State of ——. (Seal.)

The State of Texas,
County of Hidalgo:

Before me, the undersigned, a Notary Public in and for said County and State, on this day personally appeared —— ——, known to me to be the person and officer whose name is subscribed to the foregoing instrument and acknowledged to me that the same was the act and deed of the said Pummill Management Company, a corporation, and that he executed the same as the act of such corporation for the purposes and consideration therein expressed, and in the capacity therein stated.

Given under my hand and seal of office this the — day of ————, A. D. 19—.

—— ——, Notary Public in and for Hidalgo County, Texas. (Seal.)

[fol. 53] 3. The plaintiff Emery C. Blackwell made two purchases of land from Pummill Development Company

comprising a total of 80 acres. This land is described in plaintiffs' complaint on file herein. Citrus trees have been planted on his initial 40 acre purchase but no care or management contract has been executed between Emery C. Blackwell and Pummill Management Company on this tract. The second 40 acre purchase was of open land to which no citrus trees have been planted and no care or management contract was ever entered into between Emery C. Blackwell and Pummill Management Company as to this tract of open land.

(S.) Carl Pummill.

State of Texas,
County of Hidalgo:

I have read the foregoing. The facts contained therein are known to me to be true.

(S.) Carl Pummill.

Sworn to and subscribed before me this 13th day of October, 1951. (S.) Scott Martin, Jr., Notary Public, Hidalgo County, Texas. (Seal.)

[fol. 54] In United States District Court

Memorandum Opinion—Filed April 1, 1952

Smith, McIlheran & Smith, Weslaco, Texas, Attorneys for Plaintiff.

Hill, Lochridge & King, Mission, Texas; Kelley, Looney, McLean & Littleton, Sidney L. Farr, Edinburg, Texas, Attorneys for Defendants.

Louis T. Loss, Associate General Counsel; Alexander Cohen, Special Counsel, Securities and Exchange Commission, 425 Second Street, N. W., Washington, D. C., Amicus Curiae.

Memorandum

Eight Texas plaintiffs sue fifteen Texas defendants, claiming the right to maintain this action as a class suit, in

spite of the lack of diversity of citizenship, under the Securities Act of 1933. Plaintiffs allege in substance that:

[fol. 55] Defendants conspired to defraud members of the buying public, and plaintiffs in particular, by selling *securities* and/or investment *contracts* in violation of Sections 77 1(2) and 77q of said Securities Act of 1933;[1] in carrying out the scheme, defendants acquired an 800 acre tract of land in Hidalgo County, Texas, prepared it to resemble irrigated citrus land and sold it, in small tracts, as such to plaintiffs and other members of the buying public residing outside of the Rio Grande Valley and unfamiliar with the true facts at prices far above its actual value, together with a property management or care contracts, *the whole transaction being treated as an investment by both buyer and seller;*

Through the *care contracts*, defendants continued to extract money from plaintiffs under continuing false and fraudulent representations that (the) representations previously made were true and that the investment was sound and was appreciating in value through such continuing investment and through affirmative acts of concealment of the true facts; such sales of *securities* and/or *investment contracts* were made by false and fraudulent representations and concealment of material facts; each defendant performed a part in carrying out the conspiracy and executed and perpetrated the fraud on plaintiffs in connection with certain sales of *securities* and/or *investment contracts* executed by defendants Pummill Development Company and Pummill Management Company as sellers and plaintiffs as purchasers;

Pursuant to the plan and scheme, plaintiffs purchased on various dates ranging from November 23rd, 1949 through March 3rd, 1950, said *securities* and/or *investment contracts in the form of 20 acre tracts* (except plaintiff, Emery C. Blackwell purchased *two 40-acre tracts), described by lot and block numbers in the Rio Grande Development Company's Subdivision in Hidalgo County*, agreeing to pay generally $400 per acre,[2] some in cash and any balance

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[1] Really Sections 12(2) and 17 of the Securities Act, 15 U. S. C. A. 77 1(2) and 77q.

[2] Plaintiff Weatherly agreed to pay $360.00 per acre.

by 5% notes; each generally also paid $2500.00 in cash for each 20 acres to have it planted to young citrus trees and various sums in investigating said investments and discovering the true facts.

The *purchase contract* in each instance was executed by defendant, Carl Pummill, President of defendant, Pummill Development Company (a corporation), and a particular plaintiff; a warranty *deed* subsequently *issued on the same date*[3] and was filed for record; in each instance shortly [fol. 56] thereafter defendant, Pummill Management Company (a corporation) executed and delivered to each plaintiff a *care contract*, agreeing to care for the property for five years, with each plaintiff to continue to invest money in such property *through such care* by depositing sufficient sums from time to time in the First National Bank of Mission, Texas, to the joint account of each particular plaintiff and the management company; *the deeds and care contracts as well as monthly statements on the investment to be made in the care fund were forwarded to each plaintiff through the United States mails;* each plaintiff had invested a stated total amount in said security and had had no return of any kind thereon;

Plaintiffs were induced to sign said *investment contracts* and/or *purchase agreements* because of reliance upon false and fraudulent representations, or fraudulent concealment, resulting from the cumulative effect of the acts of defendants pursuant to the conspiracy, as follows:

By investment in said citrus development, *plaintiffs could get in on an 800 acre unit which would be developed by one company in a uniform manner, under the management of citrus experts, for the joint benefit of all investors;* at the end of three years the property would be paying all of its own expenses; after five years, it would produce a minimum return of 20%; the property was in Water District 7 and, while no canals were then on the property, they would be extended within 18 months; the citrus trees would be tank watered in the meantime; the land was some of the best citrus land in the Rio Grande Valley, was being sold at the

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[3] A correction deed was issued later to plaintiff, Boyd Construction.

pre-war price of $400.00 per acre and, if not bought now, would not be available at that price; it was worth more and land equally as good in the Valley could not be bought for that price; only the finest citrus stock would be used in planting; the investor would not have anything to worry about, the management company would take care of everything and the investor could sit back and reap the dividends; the investor was getting only ⅛ of the customary ⅛th mineral interest because that was all the development company had in the minerals; good citrus water was being put on the trees since bills for water were sent each month prior to their additional *investments in care* for said trees;

After the oral false representations were made, defendants forwarded the *deeds, contracts* and *statements* to plaintiffs through the United States mails and *continued to make false representations by sending plaintiffs through the mails care bills, including charges for* irrigation water which was neither used (by) nor available to defendants for such use.

[fol. 57] Sometime during the months of February, March and April, 1951, plaintiffs jointly discovered that the foregoing representations were false; by virtue of the misrepresentations, defendants violated Sections 77 1(2) and 77q of the Securities Act and were liable to plaintiffs for return of the money and property expended in their investment.[4]

Plaintiffs tender return of the investment contracts or securities and the land. After pleading particular acts

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[4] The Securities and Exchange Commission exphasizes in the Amicus Curiae brief that it makes no independent assertions with respect to the facts alleged by plaintiffs. Its brief is filed on the basis that the allegations in the complaint are admitted as true on motion to dismiss. In five similar cases filed against the same principal defendants here, (in which jurisdiction was grounded on diversity of citizenship), practically the same allegations of conspiracy and fraud were made. After a jury trial lasting nearly four weeks, there were findings of no conspiracy and a hung jury on the issue of fraud by the selling company.

performed by each defendant, "either directly or as co-conspirators, agents, employees or by agreement," plaintiffs pray for cancellation and return of their money, exemplary damages and costs (including attorneys fees). In the alternative, if the court should deny recovery under the Securities Act then for relief under Texas laws.

Defendants move: (1- to dismiss (a) for want of jurisdiction; (b) for failure to state a claim; (2) to dismiss (a) because the action cannot be brought as a class action; (b) for misjoinder of parties, both plaintiffs and defendants; and (3) for more definite statement.

[fol. 58] Defendants' motion to dismiss for want of jurisdiction is based on two propositions which will be discussed as stated.

First: the transactions alleged do not constitute a "security" [5] within the meaning of the act. Many cases are cited and discussed in the briefs—too many to discuss and distinguish here. It is clear that plaintiffs have framed their complaint with an eye to S. E. C. v. W. J. Howey Co. et al., 328 U. S. 293. In the words of counsel for defendant, Pummill: "These residents of Texas, having read some cases and being anxious to secure Federal jurisdiction for trial of land fraud suits have plead in a manner calculated to obtain Federal jurisdiction" Plaintiffs almost succeed in doing this; but, for reasons hereafter set out, I hold they have not.

Pummill has filed an affidavit with his brief, setting out the provisions of the muchly referred to care contracts which were on mimeographed forms. Since these provisions are not disputed, they will be considered as part of the motions to dismiss which, in turn, will be considered [fol. 59] as speaking motions.[6]

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[5] Sec. 2(1) of the Securities Act, 15 U. S. C. A. 77b(1) provides so far as applicable here, as follows: "The term 'security' means any note, stock, . . . investment contract . . . or, in general, any interest or instrument commonly known as a security. . . ."

[6] The care contracts recite and provide:

A named plaintiff is the owner of a described lot of land containing 20 or 40 acres; he contracts with the manage-

[fol. 60] In many respects the facts alleged here are similar to those established in the Howey case; but the *controlling* facts are not the same. ". . . an investment contract for the purposes of the Securities Act means a contract, transaction or scheme whereby a person invests his money in a *common enterprise* and is led to expect profits *solely* from the efforts of the promoter or a third party . . . The test is whether the scheme involves an investment of money in a *common enterprise* with profits to come solely from the efforts of others," S. E. C. v. Howey Co., supra. (Emphasis supplied). That case further says that it must be something more than fee simple interests in land, something different from a farm or orchard coupled with management services.

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ment company to supervise the care of the grove located on his land for one year and to continue from year to year for five years; with the owner being privileged to terminate the arrangement upon 30 days written notice, if all amounts due the care company are paid; the company likewise may terminate on 30 days written notice in January of any year;

The owner pays $1.00 a month per acre in advance for management and the cost of all labor materials, water, seed, etc., (fertilizer and crop cover, not to be used, however, except as directed by the owner); a fund in a stated amount for these costs is to be established in a designated bank, the management to have authority to draw checks thereon for labor, materials and compensation and being required to account for all amounts expended; the owner is to replenish the account within 10 days after each accounting, but has the right to withdraw the deposit upon 10 days written notice; if the owner fails to make such deposits within 30 days of an accounting, the care company is released from all liability and has the right to cancel but the owner remains liable for all amounts due up to the termination date;

The term "care" obligates the management company to do everything it believes to be necessary and to the best interest of the owner, including enumerated acts in the cultivation of the grove and care of the trees; the com-

In the Howey case, Howey kept half of the groves, offering the other half to the public *to finance additional development*. There is no such claim here. Nor is it claimed that prospective investors were told it was not feasible to invest in a grove unless service arrangements were made as in Howey. There is a vast difference in buying narrow, unmarked strips averaging 1.33 acres as in Howey and buying 20 and 40 acre tracts,[7] described by lot and block number, as here.

[fol. 61] The service contract could not be cancelled in Howey; here it can. There the owners had no right of control or possession for 10 years or right of suggestion as to care and cultivation; here they have such rights. All the produce from the entire Howey project was *pooled*, the owners' share of the net profits being determined by the ratio of his minute acreage to the whole. Here the owner is entitled to sell the produce from his 20 or 40 acres to others if he so desires. His profits are not dependent on the yield from or cost of producing or marketing the produce from any other tract.

While plaintiffs have alleged that it was represented to them that they were getting in on an 800 acre unit to be developed under one management for the benefit of all the

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pany is to use its own best judgment and, in addition, do any other care work requested by the owner;

The company is to be liable for its own negligence but not for the acts of God, shortage of water or materials, etc.; any necessary change in care or charges to be made after mutual agreement; the company is to be responsible for harvesting and marketing of all fruit produced and will use due diligence in that respect; but the owner must notify the company in writing, prior to marketing, as to his preference in that respect and whether he has made a sales agreement with others; in the latter event, the company is to give full co-operation and keep a complete account of such harvesting and marketing and remit to the owner, less 5%;

All amounts due by the owner to bear interest at 5%, attorneys fees and a crop lien being provided for.

[7] A large "ranch" in California, a good sized citrus farm in the Rio Grande Valley.

investors, there is no suggestion in the care contracts of joint development, operation or relation to any other acreage. The allegations are that a purchase agreement was executed and a warranty deed issued *on the same date and filed for record.*[8]

Plaintiffs' allegations, in the light of the actual terms of the care contracts, fall far short of showing an investment in a common enterprise. This is, in reality, a number of actions, combined in one, for alleged fraud in the sale of lands; and, perhaps, for breach of contract for orchard [fol. 62] management. I do not believe that the Securities Act was designed to reach the transactions here revealed.

Defendants' first point will be sustained.

Second: Defendants contend that even though the transactions alleged constitute investment contracts, or securities, they do not come within the prohibitions of Sections 12(2) of the Securities Act since the only allegations as to use of the mails is that the deeds, care contracts and monthly statements on the care contracts were mailed to plaintiffs after alleged oral misrepresentations and concealments, and after consummation of the sale.

Section 12(2), 15 U. S. C. A. 77, 1(2), creating a civil remedy in behalf of purchasers of securities, reads, so far as applicable here, as follows:

> "Any person who . . . (2) sells a security . . . by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could

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[8] The date of filing of recording is not given. This may be significant and may explain the allegation as to the *deed* being sent to each plaintiff by mail after consummation of the purchase, since it is prudent, that a deed should be recorded promptly by the purchaser or some one for him.

not have known, of such untruth or omission, shall be liable to the person purchasing such security from him. . . ."[9]

[fol. 63] Defendants contend that it is not enough that the contracts, deeds and monthly statements were mailed to plaintiffs after oral communication; that, in addition, a prospectus must have been transmitted by mail or by means of interstate transportation or communication (since obviously an oral communication cannot be transmitted by mail, although it could by interstate radio or telephone). Plaintiffs, on the other hand, joined by amicus curiae, contend that it is sufficient if there be oral misrepresentations and the mails are used in any manner in connection with the sale or in delivering the deeds, care contracts or monthly statements—just as though a civil remedy had been created by Section 12(2) for victims of a scheme to defraud in the sale of a security where the mails are used in any manner in its execution as under the mail fraud statute[10] or the criminal provisions of Section 17 of the Securities Act.

There is authority for both views[11] but no decision in this circuit. No useful purpose would be served by detailed discussion on my part.

[fol. 64] Kemper v. Lohnes, 7th Cir., 173 F. (2d) 44, summarizes my problem and best represents my views. It discusses the cases relied upon by plaintiffs. In spite of the criticism leveled at the decision by amicus curiae, it seems

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[9] Jurisdiction is conferred by Sec. 22(a); 15 U. S. C. A. 77V.

[10] 18 U. S. C. A. 1341.

[11] Defendants rely on: Kemper v. Lohnes, 7th Cir., 173 F. (2d) 44; Independent Sharps Corp. v. Deckert, 3rd Cir., 108 F. (2d) 51; Murphy v. Cady (D. C. Me.) 30 F. Supp. 466, 469; Cross v. Independence Shares Corp., (D. C. Penn.) 36 F. Supp. 541.

Plaintiffs rely on: Schiller v. H. Vaughan Clarke & Co., 2nd Cir., 134 F. (2d) 875; Moore v. Gorman (D. C. N. Y.) 75 F. Supp. 453.

Comments in various law reviews and articles supporting both views have been cited by amicus curiae.

to me to be well reasoned. I content myself therefore by quoting from it as follows:

> "The cases reveal that a number of courts have been confronted, as we are, with interpreting the rather confusing phraseology which Congress has employed and, as might be expected, have reached different results. We do not regard any of the cases which we have read as particularly helpful and it seems to be one of those instances where each court confronted with the problem must make its own appraisement of the statutory language.
>
> (1) The phraseology of the section as applied to the pertinent allegations of the complaint may be reduced to read that any person who 'sells a security . . . by the use . . . of the mails, by means of . . . oral communication . . .' This must be so because it is not claimed that 'any means or instruments of transportation or communication in interstate commerce' was used other than that of the mails, nor is it claimed that there was any untrue statement 'by means of a prospectus.' The untrue statement, as alleged, was by means of an 'oral communication.' Of course, it is evident that an untrue statement made by 'oral communication' cannot take place through the mails, which we think indicates that the section does not contemplate the inclusion of an 'oral communication' in connection with 'use of the mails.' "
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> [fol. 65] "(2) Now to approach the matter from another angle. Assuming that an 'untrue statement' is the gravamen of the cause, as we think it is and as was stated in Pennsylvania Co., etc. v. Deckert et al., 3 Cir., 123 F. 2d, 879, 984, such untrue statement must be made either (1) 'by means of a prospectus' or (2) by 'oral communication,' and in turn these two means of imparting an untrue statement must be made (1) 'by the use of any means or instruments of transportation or communication in interstate commerce' or (2) 'by the use . . . of the mails.' It appears to us, in fact we think it unreasonable to think otherwise, that 'by the use . . . of the mails' was employed solely in connection with 'by means of a prospectus', as the

latter term is defined in the Act. Sec. 77b (10) states: 'The term "prospectus" means any prospectus, notice, circular, advertisement, letter, or communication, written or by radio . . .' Thus the matters included in this definition are written and such as are commonly sent through the mails. An oral communication cannot be sent through the mails, and it is unrealistic to associate such a communication with the use of the mails.

"Of course, the phrase 'oral communication' must be recognized and given a place in construing the section, but that may be done by associating the term with a means of 'communication in interstate commerce'. Sec. 77b(7) states: 'The term "interstate commerce" means trade or commerce in securities or any transportation or communication relating thereto among the several States . . .' This certainly would include telephone conversations as means of communication in interstate commerce and perhaps broadcasts by radio, and these [fol. 66] two means of 'oral communication' alone might well include a large segment of the communications in interstate commerce which Congress intended to reach.

"The case most strongly relied upon by plaintiff, which admittedly furnishes support for her contention, is Schillner et al. v. H. Vaughan Clarke & Co. et al., 2 Cir., 134 F. 2nd 875. In that case the misrepresentations were oral and were made by a Philadelphia stock broker in conversation with the buyers, in Rome, New York. Liability was held to exist under Sec. 12(2), since the stock certificates were delivered by mail from defendant's Philadelphia office to the plaintiffs in Rome, New York. That case is distinguishable in that there, while the untrue statements which resulted in the sale were made by oral communication, the sale was not actually consummated until the certificates were delivered, and delivery was made by mail, while in the instant situation the most that can be said for the use of the mail is that the parties exchanged letters which resulted weeks later in a meeting where the untrue

statements were made. This distinction in the facts, it may be admitted, does not distinguish the reasoning which the court there employed. The court, however, conceded, 134 F. 2d page 877, that its construction of the statute was not in accord with the weight of judicial authority (citing cases which had held to the contrary). Our construction of the statute compels us, also, to take issue with the result reached in that case.

[fol. 67] "(3) In our judgment, the alleged misrepresentations which were made by means of 'oral communication' were not made 'by the use . . . of the mails' and, therefore, no cause of action was stated."

In addition it is to be noted that Section 12(1) creates the same civil remedy against any person who "sells a security in violation of Section 5" (15 U. S. C. A. 77e). Section 5 makes it unlawful, unless a registration statement is in effect, among other things, "to cause . . . to be carried through the mails . . . any such security for the purpose of sale or for *delivery after sale.*" Whatever the reasons, it thus appears that Congress has specifically provided in actions under Sections 12(1) and 5 that it is unlawful to *deliver* the security through the mails and significantly, has failed to so provide in actions under Section 12(2). There are other differences between the language employed in Section 12(2) and in Section 17 and other sections which to my mind distinguish the many criminal cases upholding almost any incidental use of the mails in connection with a sale or in furtherance of a fraudulent scheme.

Defendant's second jurisdictional point also will be sustained.

In view of this disposition it is unnecessary to discuss the remaining questions raised by defendants. Since all plaintiffs and all defendants are resident citizens of Texas, the Court has no power to grant plaintiffs' alternate prayer for relief under Texas laws.

[fol. 68] I regret that the pressure of constant trial work for the past three months has prevented detailed discussion of the many cases and points advanced in the briefs. I desire, however, to express particular appreciation for the able and exhaustive brief filed by amicus curiae.

The Clerk will notify defendants' counsel to submit an order in accordance with this memorandum.

(S.) James V. Allred, Judge.

Corpus Christi, Texas,

March 31st, 1952.

[fol. 69] IN UNITED STATES DISTRICT COURT

ORDER OF DISMISSAL FOR LACK OF JURISDICTION—Entered April 10, 1952

Be it remembered that in the above entitled and numbered cause on the 31st day of March, 1952, the Court rendered its judgment on the consolidated motions theretofore timely filed and properly presented by the Defendants through their attorneys of record, the said consolidated motions consisting of those filed respectively for the several defendants and including consolidated motions of Defendants Lloyd M. Bentsen, Sr., Elmer C. Bentsen, and Bentsen Development Company filed by their attorneys of record, Kelley, Looney, McLean & Littleton of Edinburg, Texas, consolidated motions of Defendants Earl Pummill, Carl Pummill, Albert L. Richter, C. W. Norton, L. H. Ramey, R. B. Kale, Pummill Development Company and Pummill Management Company filed by their attorneys of record, Hill, Lochridge & King of Mission, Texas, and consolidated motions of the Defendant G. F. Dohrn through adoption of the consolidated motions of the other defendants and filed by himself, and presented to the Court Motions (1) to dismiss for want of jurisdiction, (2) to dismiss for failure to state a claim upon which relief could be granted, (3) to dismiss because the action could not be brought as a class action, (4) to dismiss for misjoinder of parties Plaintiffs [fol. 70] and Defendants, and (5) alternative motion for a more definite statement; and the motions having been timely placed upon the motion docket and properly submitted to the Court, and the parties having filed their respective and several briefs on the said motions, and there having been filed an Amicus Curiae brief on behalf of the Securities and Exchange Commission after leave granted

by the Court; and the Court having considered the said motions, the briefs and all matters filed in support of or in opposition thereto by the respective parties, was of the opinion that the Defendants' Motion to Dismiss for Lack of Jurisdiction was well taken and should be sustained; and the Court was of the further opinion that having decided to sustain the Defendants' Motion to Dismiss for Lack of Jurisdiction, it is unnecessary to enter any order on the several other matters filed by the Defendants, and the Court being of the opinion that the said cause should in all things be dismissed for want of jurisdiction;

It is, therefore accordingly, ordered, adjudged and decreed by the Court that the said entitled and numbered cause wherein Emery C. Blackwell, Boyd Construction Company, Claude E. Blackwell, Clyde W. Weatherly, Arie K. Smith, Dudley Smith, W. H. Ham, Herbert Clark, and Frank L. Danner are the Plaintiffs, and Lloyd M. Bentsen, Sr., Elmer C. Bentsen, G. F. Dohrn, Albert L. Richter, R. B. Kale, Earl Pummill, Carl Pummill, C. W. Norton, C. A. [fol. 71] Connor, L. H. Ramey, Allen Beckham, Pummill Development Company and Pummill Management Company are the Defendants, shall be, and the same is hereby, in all things dismissed for lack of jurisdiction; and the costs of said cause are assessed against the Plaintiffs for which the Officers of the Court may have their execution.

Entered this 10 day of April, 1952.

(S.) James V. Allred, Judge, U. S. District Court, Southern District of Texas, Brownsville Division.

IN UNITED STATES DISTRICT COURT

NOTICE OF APPEAL—Filed May 8, 1952

Notice is hereby given that Emery C. Blackwell, Boyd Construction Company, Claude E. Blackwell, Clyde W. Weatherly, Arie K. Smith, Dudley Smith, W. H. Ham, Herbert Clark and Frank Danner, plaintiffs in the above entitled and numbered cause, hereby appeal to the United States Circuit Court of Appeals for the 5th Circuit, from the

Final Order of Dismissal for Lack of Jurisdiction, entered [fols. 72-76] in this action on April 10, 1952.

Smith, McIlheran & Smith, By (S.) E. H. McIlheran, Attorneys for the Plaintiffs-Appellants, 516 Texas Boulevard, Weslaco, Texas.

Bond on appeal for $250.00 filed May 8, 1952, omitted in printing.

[fol. 77] In the United States District Court

Stipulation Designating Parts of Record to Be Presented —Filed May 13, 1952

It is hereby stipulated that the following shall comprise the record on appeal of the above entitled cause to the United States Circuit Court of Appeals for the 5th Circuit:

1. Complaint (erroneously designated Plaintiffs' Original Petition).
2. Consolidated Motions of Defendants Lloyd M. Bentsen, Sr., Elmer C. Bentsen and Bentsen Development Company.
3. Consolidated Motion of Defendant Earl Pummill, Carl Pummill, Albert L. Richter, C. W. Norton, L. H. Ramey, Pummill Development Company and Pummill Management Company.
4. Motion of R. B. Kale.
5. Motion of G. F. Dohrn.
6. Motion of Frank L. Danner to Intervene as Plaintiff.
7. Order granting Frank L. Danner leave to intervene.
8. Affidavit attached to brief of Earl Pummill, et al, [fol. 78] treated by District Court as Speaking Motion.
9. Memorandum Opinion.
10. Order of Dismissal for Lack of Jurisdiction.

It is further stipulated that the above record may be printed by the Appellants prior to its transmission to the United States Circuit Court of Appeals for the 5th Circuit.

Dated this 30th day of April, 1952.

Smith, McIlheran & Smith, By (S) E. H. McIlheran, Attorneys for the Plaintiffs, Weslaco, Texas, Hill, Lochridge & King, By (S) L. P. Lochridge, Jr., Attorneys for the Defendants, Earl Pummill, Carl Pummill, Albert L. Richter, C. W. Norton, L. H. Ramey, R. B. Kale, Pummill Development Company and Pummill Management Company, Mission, Texas, Kelley, Looney, McLean & Littleton, By (S) Jackson Littleton, Attorneys for the Defendants, Lloyd M. Bentsen, Sr., Elmer C. Bentsen, Bentsen Development Company and G. F. Dohrn.

[fol. 79] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 80] IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

ARGUMENT AND SUBMISSION—November 27, 1952.

(Omitted in printing)

[fol. 81] IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 14127

EMERY C. BLACKWELL, et al., Appellants,

versus

LLOYD M. BENTSEN, SR., et al., Appellees

Appeal from the United States District Court for the Southern District of Texas

April 27, 1953

Before Holmes, Russell and Strum, Circuit Judges

OPINION OF THE COURT—Filed April 27, 1953

STRUM, Circuit Judge:

The basic question presented by this appeal is whether or not the district court erred in dismissing the complaint for lack of federal jurisdiction. This in turn involves two constituent questions: (1) Do the transactions described in the complaint constitute "investment contracts" as contemplated by sec. 2(1) of the Securities Act of 1933, 15 U. S. C. A. 77(b)(1); and (2) Does the use of the mails in [fol. 82] consummating these transactions entitle plaintiffs to relief under sec. 12(2) of said Act, 15 U. S. C. A. 77*l*(2). The district judge answered both these questions negatively.

There is no diversity of citizenship. Federal jurisdiction depends entirely upon alleged violations of the Securities Act of 1933.

In substance, the complaint alleges that during the latter part of 1949 and early 1950, each of the 9 appellants, plaintiffs below, purchased lands, usually in units of 20 acres, from Pummill Development Company, one of the defendants below, for the purpose of developing the same into small citrus groves. These small tracts were parts of an 800 acre tract owned by the Development Company, and said to be suitable for citrus cultivation.

Concurrently with, or shortly after, executing the land purchase contract with Pummell Development Company,

the purchaser also executed a care and management contract with Pummill Management Company, under which the latter agreed to plant young citrus trees on the land, cultivate and develop the grove, harvest and market the crops, and remit the proceeds to the owner, after deducting 5% of the proceeds as compensation for harvesting and marketing services. A separate consideration was paid for planting the trees. While the Management Company undertook full responsibility for harvesting and marketing the crops in the absence of directions from the owner, the management contract contained provisions for an investor to give directions as to the marketing of the crop on his tracts, in which event the Management Company would [fol. 83] follow these directions but would apparently still supervise the harvesting and marketing and would still receive its compensation therefor.

The defendants Earl and Carl Pummill were the organizers of the two Pummill companies, and are directors and stockholders therein. The purchase contract for the land, and the accompanying management contract, were in each instance executed by Carl Pummill, who was president of both companies. The management contracts usually covered a period of one year, with the option to renew annually up to five years.

Appellants, and most of the other purchasers, were inexperienced in citrus culture and resided outside the Rio Grande Valley of Texas in which these lands were located. Prospective purchasers were induced by salesmen of the vendors to visit the vicinity of the lands where they were entertained by the vendors, and taken on a tour of the lower Rio Grande Valley. They were told by the vendors that "by investing in this citrus development * * * they could get in on an 800 acre unit which would be developed by one company in a uniform manner, and under the management of citrus experts, for the joint benefit of all investors," and that "they would not have a thing to worry about; that the Management Company would take care of all problems which might arise, and the investor would only have to sit back and reap the dividends." It was further represented that the property would be paying all of its expenses in 3 years, and that the investment would produce a minimum return of 20% per annum after 5 years.

[fol. 84] Investors would usually buy one or more 20 acre tracts on one of these visits, and a deed or contract therefor, and the management contract to accompany the same, would be later mailed to the purchasers at their homes. Plaintiffs allege that they were induced to purchase these lands, and enter into management contracts, by fraudulent misrepresentations and concealment of material facts concerning the character, quality and value of the land sold, and in other respects.

With the two possible exceptions hereinafter mentioned, these are in principle the same type of purchase-management contracts which have been held by the Supreme Court to be "investment contracts" within the meaning of sec. 2(1) of the Securities Act of 1933. *Securities & Exch. Comm. v. W. J. Howey Co.*, 328 U. S. 293, 90 L. Ed. 1244; *Securities & Exch. Comm. v. C. M. Joiner Leasing Corp.*, 320 U. S. 344, 88 L. Ed. 88. See also *Securities & Exch. Comm. v. Bailey*, 41 Fed. Supp. 647, decided prior to the *Joiner* and *Howey* cases.[1] In the *Howey* case, *supra*, the court held that in using the term "investment contract" in the Securities Act, Congress employed a term the meaning of which had been crystallized by prior judicial interpretations, and that the term covered contracts of the type here [fol. 85] involved. We notice minor and non-determinative differences between the facts of this case and those in the

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[1] Note. Many other courts have taken the same view. Amongst the decisions are: Securities & Exchange Comm. v. Tung Corp. of America, 32 Fed. Supp. 371; Kerst v. Nelson, 213 N. W. 904, 54 A. L. R. 495; State v. Evans, 191 N. W. 425, 27 A. L. R. 1165; State v. Gopher Tire Co., 177 N. W. 937; State v. Agey, 88 S. E. 726; Webster v. United States I. Realty Co., 212 N. W. 806; Prohaska v. Hemmer-Miller Co., 256 Ill. App. 331; In re: Waldstein, 291 N. Y. S. 697; Note, 87 A. L. R. 82. Securities & Exch. Comm. v. Crude Oil Corp., 7 Cir., 93 Fed. (2) 844; Securities & Exch. Comm. v. Payne, 35 Fed. Supp. 873; Securities & Exch. Comm. v. Universal Service Ass'n., 7 Cir., 106 Fed. (2) 232; Securities & Exch. Comm. v. Wickham, 12 Fed. Supp. 245; Gracchi v. Friedlander, 270 P. 235. Cf. contra, State v. Hamphill, 142 Fla. 728, 195 So. 915.

Howey and *Joiner* cases, but the determinative factors are in principle the same.

Here, as in the *Howey* and *Bailey* cases, *supra*, the sales and management contracts, though separate in form and execution, are closely allied in performance, as well as in personnel. They form constituent parts of what is essentially one transaction. In essence, what the defendants are really offering, and certainly what the average purchaser is really buying is, not land for its intrinsic value as such, but a producing orange grove as a source of income, without which they would not be interested in purchasing the land. Purchase of the land is merely the conduit through which the investment is accomplished. Instead of a stock certificate evidencing a share in a common ownership of capital assets, these purchasers receive a deed evidencing an ownership in severalty. But the paramount emphasis is upon the income to accrue, which is the chief, if not the sole, attraction to the purchaser. Based upon the defendants' representations, the purchaser's expectation is that for a sum of money invested in a small tract of land which the purchaser places in the hands of the defendants for cultivation along with many similar and contiguous tracts owned by others, he will ultimately receive an income from the yield produced by defendants' developing and managing activities. This is not an ordinary purchase of land as such. It is an investment for the purpose of producing an income through the activities of others than the owner. Consequently the transactions constitute "investment contracts" within the meaning of that term as defined in the *Howey* case, and other cases, *supra*.

[fol. 86] It is significant that few, if any, of these small tracts are purchased by citrus farmers who wish to cultivate them as a personal farming enterprise. The overwhelming percentage of purchases are by persons who are inexperienced in citrus cultivation, who live at a great distance from the lands, and who apparently have no intention of occupying the land or cultivating it by their own efforts, but who are attracted thereto solely by the income to be derived through cultivation of the land by the Management Company.

There is a dispute of fact as to whether two of the purchasers here involved entered into management contracts.

If they merely purchased land, without more, such a purchase would not constitute an investment contract within the meaning of the Securities Act. In view of the dispute on this point, we leave that question open for decision on the facts as they develop at the trial. As to all those, however, who executed care and management contracts in connection with their contract of purchase, we hold on the authority of the cases above cited, that the transactions constitute "investment contracts" within the meaning of sec. 2(1) of the Securities Act of 1933. At least as to these, the complaint should not have been dismissed.

Though the mails are not alleged to have been used for the purpose of sending out prospectuses or advertising these lands for sale, all deeds and management contracts by which the transactions were consummated were returned by the vendors to the purchasers through the mails. We are aware of the conflict in the authorities on the subject, but in our opinion this is a sufficient use of the mails to [fol. 87] bring the case within sec. 12(2) of the Act. This is a remedial statute. It should be liberally construed to accomplish the dominant legislative purpose in adopting it, which is to prevent the use of the mails, and other instrumentalities of interstate commerce, in the perpetration of investment frauds. Sec. 12 of the Act, so far as here material, provides: "Any person who * * * sells a security * * * by the use of * * * the mails, by means of a prospectus *or oral communication*, (Italics supplied) which includes an untrue statement of a material fact * * * shall be liable to the person purchasing the security from him * * *." Here the sales were apparently by oral communication, but the transactions were consummated by the use of the mails, which in our opinion brings the transaction within the statute. Delivery of the deeds and contracts is an integral part of the sale. *Schillner v. H. Vaughan Clarke & Co.*, 2 Cir., 134 Fed. (2) 875, 165 A. L. R. 1232 (note); *Moore v. Gorman*, 75 Fed. Supp. 453. Compare, *contra*, *Kemper v. Lohnes*, 7 Cir., 173 Fed. (2) 44, which was followed by the district court.

Since at least some, if not all, of these transactions are within the purview of the Securities Act, federal jurisdiction exists and the complaint should have been retained.

Reversed and remanded.

[fol. 88] IN UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 14127

EMERY C. BLACKWELL, et al.,

versus

LLOYD M. BENTSEN, SR., et al.

JUDGMENT—April 27, 1953

This cause came on to be heard on the transcript of the record from the United States District Court for the Southern District of Texas, and was argued by counsel;

On consideration whereof, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, reversed; and that said cause be, and it is hereby, remanded to the said District Court for proceedings in accordance with the opinion of this Court;

It is further ordered and adjudged that the appellees, Lloyd M. Bentsen, Sr., and Others, be condemned, in solido, to pay the costs of this cause in this Court, for which execution may be issued out of the said District Court.

[fols. 89-98] Petitions for rehearing covering 10 pages filed May 16, 1953 omitted from this print. They were denied, and nothing more by order July 27, 1953.

[fol. 99] IN UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

[Title omitted]

ORDER DENYING REHEARING—July 27, 1953

It is ordered by the Court that the Petitions for Rehearing filed in this cause be, and the same are hereby, denied.

[fols. 100-101] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 102] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., et al., Petitioners,

vs.

EMERY C. BLACKWELL, et al.

ORDER ALLOWING CERTIORARI—Filed December 7, 1953

The petition herein for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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FILED
OCT 21 1953
HAROLD B. WILLEY, Clerk

Supreme Court of the United States

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., *et al.*,
Petitioners,

v.

EMERY C. BLACKWELL, *et al.*,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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October, 1953.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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Supreme Court of the United States

OCTOBER TERM, 1953

No.

LLOYD M. BENTSEN, SR., *et al.*,
Petitioners,

v.

EMERY C. BLACKWELL, *et al.*,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

TO THE HONORABLE, THE CHIEF JUSTICE OF THE UNITED STATES, AND TO THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Come now the petitioners, Lloyd M. Bentsen, Sr., Elmer C. Bentsen and Bentsen Development Company, and pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit entered in the above entitled case on April 27, 1953.

OPINIONS BELOW

The memorandum opinion of the District Court (R. 54-68) and the opinion of the Court of Appeals (R. 81-87) are both unreported.

JURISDICTION

The judgment of the Court of Appeals was entered on April 27, 1953 (R. 88). Petitions for rehearing were denied on July 27, 1953 (R. 99). The jurisdiction of this Court is invoked under 28 U. S. C. § 1254 (1).

QUESTION PRESENTED

This is a local land dispute in which purchasers of citrus land in the Rio Grande Valley of Texas seek to invoke federal jurisdiction by pleading § 12(2) of the Securities Act of 1933, 15 U. S. C. § 77*l*(2). Does this Section apply to a purely intrastate transaction where the sale is completed without the use of the mails or interstate commerce, but some time thereafter the executed documents evidencing the completed transaction are forwarded by mail to the purchasers?

STATUTE INVOLVED

Section 12(2) of the Securities Act of 1933, as amended, 15 U. S. C. § 77*l*(2) reads as follows:

"Any person who—

* * *

> sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security."

Section 22(a) of the Act, 15 U. S. C. § 77v(a) provides that the district courts shall have jurisdiction

> "concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title".

The full text of 22(a) and Section 2(1) of the Act defining "security" are to be found in the Appendix to this brief, *infra*, page 14.

STATEMENT

a. The Complaint

The present action was filed in the United States District Court for the Southern District of Texas by eight plaintiffs, residents of the State of Texas,[1] against your three petitioners, residents of the State of Texas, and twelve other residents of the same State (R. 2-3). The controversy relates to the sale of certain citrus land located in Hidalgo County, Texas, in the Rio Grande Valley. The facts are as follows:

The eight plaintiffs purchased the land in question from certain of the defendants in 20 and 40 acre lots, and paid for citrus trees planted or to be planted on their tracts. Most of the purchasers also entered into contracts with one of the defendant companies which agreed to take care of the trees in question for a specified fee and the cost of labor and material expended (R. 5-6, 8-9, 10, 11-12, 13, 14, 16).

The complaint alleged that the land in question was part of a block of 800 acres offered to persons resident "outside of the Rio Grande Valley of Texas", "together with a property management or care contract, the whole transaction being treated as an investment by both buyer and seller." (R. 4). It was then alleged that the transactions were induced by false representations of some of the in-

[1] One other Texas resident intervened as plaintiff (R. 44).

dividual defendants (R. 22, Par. VII, 3), and that the other defendants in various manners aided the said defendants (R. 21, *et seq.*, Par. VII).[2]

Plaintiffs alleged that the sale of the land coupled with the agreement to care for the land made the entire transaction the sale of an investment contract and therefore of a security under the Securities Act (R. 3-4). The decision of this Court in *Securities and Exchange Commission* v. *W. J. Howey Co.*, 328 U. S. 293, was relied on (R. 58).

The use of the mails was alleged in the following manner:

The purchase of the land was in each case made on a personal visit of the purchaser to the property in Hidalgo County, Texas,[3] and payment was made at the time. In some cases the payment was all in cash (R. 5, 15, 43) and in others by cash and notes (R. 8, 9, 11, 12, 14).[4] Deeds to the land were executed the same day and recorded in the purchaser's name (R. 8, 9, 11, 12-13, 13-14, 15-16).

On the occasion of this visit the plaintiffs purchased the land. Either the same day or later, one of the defendant companies "executed and delivered to the said Plaintiff a care contract", agreeing to care for the property (R. 8-9, 10, 11, 13, 14, 16). *The transactions were thus completely entered into and all agreements made and concluded by face to face personal discussions in Hidalgo*

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[2] In the case of your petitioners it is alleged that their participation consisted in the fact that they had been the former owners of the property and had a vendor's lien on the property (R. 21, 22, Par. VII, 1). This is accompanied by allegations that the vendor's lien was "fraudulent" and that by this means the petitioners were participating in "spoils and plunder." The other defendants are counsel who organized the land selling company, the secretary of the caretaking company, various brokers, and a bus driver for the land company.

[3] *E.g.*, as to four of the plaintiffs, it was alleged that they were induced by one of the broker defendants to make a trip from their homes in another part of Texas to the Rio Grande Valley (R. 23, paragraph 8).

[4] One purchaser traded some other land in Pecos, Texas, in part payment (R. 6, 7).

County, Texas, without use of the mails or any means of interstate commerce. No allegation or contention to the contrary is made.

In each case, however, it is alleged that the warranty deed to the property, although made out on the same date as the purchase contract, and the care contracts as well, were forwarded to the plaintiffs at their residences through the United States mail.

This is the sole basis of jurisdiction claimed and considered by the court below.[5] It was only "after" the oral representations complained of had been made and after the contracts had been entered into for the purchase of the land and care of the trees, that the mails were used to deliver copies of the documents previously executed (R. 18-19).

b. The Rulings Below

The District Court (Allred, J.) dismissed the complaint, stating:

> "It is clear that plaintiffs have framed their complaint with an eye to S. E. C. v. W. J. Howey Co., et al., 328 U. S. 293. In the words of counsel for defendant, Pummill: 'These residents of Texas, having read some cases and being anxious to secure Federal jurisdiction for trial of land fraud suits have plead in a manner calculated to obtain Federal jurisdiction.' Plaintiffs almost succeed in doing this; but, for reasons hereafter set out, I hold they have not." (R. 58.)

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[5] It was also alleged that as money was expended on care of the land, monthly care statements were sent through the mail (*e.g.*, R. 14-15, 18-19). The care statements are statements of monies expended for care of the property. Plaintiffs under their care contracts agreed to set up and did set up a fund in a local bank to be drawn on. After the money was expended a statement of the expenditure was mailed to the owner accompanied by a request to replenish the bank deposit in accordance with the contract (R. 47-48). The Court of Appeals made no mention of these mailings and apparently regarded them as too remote in time to have any connection with the sale of the alleged investment contract (R. 86, 87).

After holding that no sale of a security was alleged (R. 61-62), Judge Allred also ruled that the use of the mails was insufficient, since the alleged false statements were not made by use of the mails, and the only use of the mails was for delivery after sale (R. 62-67). He relied on and quoted extensively from *Kemper* v. *Lohnes*, 173 F. 2d 44 (CA 7, 1949).

On appeal, the Court of Appeals for the Fifth Circuit reversed on both points. It held that the complaint adequately alleged that a security was involved (except in the case of two of the plaintiffs who may not have executed care contracts) (R. 85-86). It also said that the use of the mails to deliver the "deeds and management contracts" was sufficient to bring the transaction within Section 12(2) of the Act (R. 86-87). The Court of Appeals stated: "We are aware of the conflict in the authorities on the subject, . . ." (R. 86), but it concluded:

> "Here the sales were apparently by oral communication, but the transactions were consummated by the use of the mails, which in our opinion brings the transaction within the statute. Delivery of the deeds and contracts is an integral part of the sale. *Schillner* v. *H. Vaughan Clarke & Co.*, 2 Cir., 134 Fed. (2) 875, 165 A. L. R. 1232 (note); *Moore* v. *Gorman*, 75 Fed. Supp. 453. Compare, *contra*, *Kemper* v. *Lohnes*, 7 Cir., 173 Fed. (2) 44, which was followed by the district court." (R. 87).

We submit that the Court of Appeals is in error in holding that it was sufficiently alleged that the transactions in question were investment contracts and thus securities within the Securities Act of 1933. In reaching its conclusion that Court read many things into the pleadings which in our opinion are not there. Such failure to require more precise pleading may create substantial prejudice in requiring petitioners to go through a trial to establish facts negating the existence of a security and of federal juris-

diction. Nevertheless, this question is basically one of construction of the pleadings and we do not believe that it is of sufficient consequence to merit the attention of this Court under its rules. We therefore confine this petition to the error of the court below in holding that use of the mails for incidental delivery of documents after sale is sufficient basis for federal jurisdiction under Section 12(2) of the Securities Act of 1933. If it should be necessary after action by this Court, we shall present to the trial court, after evidence, the question of the existence of a security.[6]

SPECIFICATION OF ERRORS TO BE URGED

The Court of Appeals erred:

1. In holding that delivery through the mails of warranty deeds and contracts previously executed was sufficient use of the mails to make the sale of the assumed security a sale "by the use of . . . the mails, by means of a prospectus or oral communication, which includes" a misrepresentation within the meaning of Section 12(2) of the Securities Act of 1933, and thus invoking the jurisdiction of the federal courts in an essentially local dispute.

2. In reversing the order of the District Court.

REASONS FOR GRANTING THE WRIT

1. Our contention here is simply that Section 12(2) of the Securities Act of 1933 does not apply because there was not sufficient use of the mails to meet the standards of that section. The decision of the court below to the contrary

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[6] For example, at trial, it would be established, among other things, that the allegation that the land was to be planted to "citrus" conceals the fact that each purchaser made his own managerial judgment, and had various percentages of grapefruit, valencia oranges and even tangerines planted on his land. These and other facts which have already been admitted on depositions, will, we believe, clearly establish that there is no basis for the allegation that a security is involved in these transactions, and that they are in fact ordinary land transactions. We trust, of course, that a ruling of this Court on the issue presented by this petition will make such a trial unnecessary.

and the decision of the Second Circuit in *Schillner* v. *H Vaughan Clarke & Co.*, 134 F. 2d 875 (1943), on which the court below relied, are directly in conflict with the decision of the Seventh Circuit in *Kemper* v. *Lohnes*, 173 F. 2d 44 (1949).

This conflict was conceded by the court below. It stated "We are aware of the conflict in the authorities on the subject, . . ." (R. 86) and it cited the *Kemper* case as "*contra*" (R. 87).

And indeed the Second Circuit in the *Schillner* case conceded that its view was in conflict with the existing authorities even before the *Kemper* case was decided. It stated (134 F. 2d at 877):

> "It must be conceded, however, that such expressions of judicial opinion as we have been able to find are not in accord with this view."

It then continued (ibid.):

> "In Gross v. Independence Shares Corp., D. C. E. D. Pa., 36 F. Supp. 541, at page 543, Judge Bard stated flatly that delivery of a security by mail after sale did not bring section 12(2) into play. Siebenthaler v. Aircraft Accessories Corp.,[2½] W. D. Mo. [1940], is to the same effect.[3]"

[2½] No opinion for publication. [Reported in CCH Fed. Sec. L. Rep. Par. 90, 122]

[3] In Murphy v. Cady, D.C. Me., 30 F. Supp. 466, 469, Judge Peters remarked parenthetically that the section 'applies only to inter-state communications.' A similar dictum may be found in Independence Shares Corp. v. Deckert, 3 Cir., 108 F. 2d 51, 54 where Judge Biggs described the statutory right as granted to one who has purchased securities 'upon an untrue statement of a material fact made by the use of any means of transportation or communication in interstate commerce'. See also Hearings before Committee on Interstate & Foreign Commerce on H. R. 4344, etc., 77th Cong., 2d Sess. (1941), 807, where the problem was pointed out."

This case presents a clear and admitted conflict with another Circuit on the same matter, within the meaning of Rule 38 Paragraph 5(b) of this Court.

2. The question presented is of importance with relation to private litigation under the Securities Act. The many cases cited above are, we believe, representative of a substantial body of litigation involving construction of this section. These actions have occurred in a number of Circuits. See the fact that courts in the First (*Murphy* v. *Cady, supra*), Third (*Gross* v. *Independence Shares Corp.* and *Independence Shares Corp.* v. *Deckert, supra*), Seventh (*Kemper* v. *Lohnes, supra*), and Eighth (*Siebenthaler* v. *Aircraft Accessories Corp., supra*) Circuits accord with one view, and those in the Second (*Schillner* v. *H. Vaughan Clarke & Co., supra*) (see also *Moore* v. *Gorman*, 75 F. Supp. 453 (S. D. N. Y., 1948)), and Fifth (the instant case) now hold the opposite view.

3. The question does not affect government litigation or criminal prosecutions because the section involved grants only a private civil remedy. The sections under which civil or criminal suits by the Securities and Exchange Commission and the Attorney General may be brought are much more broadly phrased. See *e.g.*, Sections 5 and 17(a), 15 U. S. C. §§ 77e and 77q(a) and Judge Allred's comment (R. 63).

4. The holding below permits controversies over local real estate transactions by the residents of a single state to be brought into the federal courts by mere ingenuity. The present case emphasizes this danger. The plaintiffs purchased real estate and arranged for care by others. Such transactions are common. They may or may not be of such a character as to be properly denominated securities transactions under the decisions of this Court. Each case depends on the facts. By careful generalities in their complaints, plaintiffs may plead the existence of a security. Under the decision below they can thus establish Federal jurisdiction. For of course almost no local real estate transaction can be carried out without some incidental use of the mails to deliver the deeds after the transaction has

been completed. The result is that, under the decision of the court below, federal jurisdiction may be extended to a great many local real estate transactions.[7]

5. The Securities Act involved a great extension of federal power. It was deemed necessary because state legislation had been ineffective to protect investors against securities sellers operating beyond the confines of a particular state.[8] A comprehensive statute was enacted providing

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[7] The effect in the instant case is clear. Judge Allred referred (R. 68) to "the pressure of constant trial work for the past three months" and noted (R. 57, n. 4):

> "In five similar cases filed against the same principal defendants here, (in which jurisdiction was grounded on diversity of citizenship), practically the same allegations of conspiracy and fraud were made. After a jury trial lasting nearly four weeks, there were findings of no conspiracy and a hung jury on the issue of fraud by the selling company."

The condition of the dockets in the other federal courts needs no elaboration. See ANNUAL REPORT OF DIRECTOR OF ADMINISTRATIVE OFFICE OF THE FEDERAL COURTS TO THE JUDICIAL CONFERENCE OF THE UNITED STATES, SEPTEMBER 1953, particularly the summary at page 1 entitled "The Still Unmet Need for More Judges."

[8] Congressional Hearings on the Securities Act of 1933 were opened by testimony of Hon. Huston Thompson who explained the need for the bill. At page 10 of the *Hearings on H. R. 4314*, March 31, 1933, he stated as follows:

> "These 'blue sky' laws of the States have failed, as is very obvious, in meeting the great problem, and that is due to a number of facts, First of all, a lack of unifomity [sic] of laws, and, second, the fact that, on the subject of extradition, those who are putting out securities can sell and send them across the State line into another State without being able to be reached so far as a criminal penalty is concerned. You only extradite and bring a man back after he has fled from a State. Well, nowadays securities can be sold from New York State over into Illinois, and the consummation of the contract can only be terminated by the consent of the seller from New York, and in that way the person in Illinois suffers if the security is not a good one; and yet the wrongful act

governmental and private remedies. Since the extent of the commerce power was not then as clear as it is now, the Act was, for constitutional reasons, based not only on the use of means or instruments of transportation in interstate commerce but also upon the use of the mails. That requirement was made disjunctive, likewise for constitutional reasons. Accordingly, although the commerce power has now been confirmed in its broadest scope, the Act in its terms applies in many instances not only to the use of interstate commerce at which it was directed, but also to intrastate uses of the mails. Where the Act is clear, the courts have of course no alternative but to apply it even to a transaction within a single state where the mails have been used. However, many provisions of the Act, including § 12(2) here involved, limit their application to a particular kind of use of interstate commerce or a particular kind of use of the mails.

Section 12(2) by its terms applies only to a sale of the security "by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes . . ." a false or misleading statement. Where it is plain that the sale was not made "by the use of" the mails or by any means or instruments of transportation in interstate commerce "by means of" a prospectus, there is no necessity in the purpose of the statute for extending its application.

Here the plaintiff Texas purchasers personally visited the site of some citrus land in the State of Texas. On these visits they purchased large blocks of that land and entered into contracts to have the land and the trees

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has been committed outside the State, and there is no way of reaching the person outside of the State."

See also *id.* at p. 99.

See also the testimony of Hon. Robert E. Healy of the Federal Trade Commission, later a Commissioner of the Securities and Exchange Commission, *Hearings on S. 875* at 214-215.

planted on it cared for. The deeds to the land were executed by the sellers and the care contract executed by the Management Company and delivered to the new owner of the land. *All this was concluded in a face-to-face transaction between Texas residents in the State of Texas in the locality where the land was located without use of any means or instrumentalities of interstate commerce or of the United States mails.* It was only *after* the transaction was concluded that at some later date the previously executed deeds to the property and the previously executed care contracts were forwarded to the plaintiffs by the United States mails.

Assuming that the sale of land and the execution of the care contract amounted to the sale of a security, how can it be said that such sale was made "by the use of . . . the mails, by means of a prospectus or oral communication, which includes" prohibited statements as required by Section 12(2)?[9] Such violence to the simple meaning of words should be applied only where Congress so intended. Cf. *United States* v. *Dickerson*, 310 U. S. 554. However, as noted above, nothing in the purposes of the Securities Act requires that its scope be extended to a controversy local in character where the local courts are fully able to grant relief.[10] It would demean the great purposes of the Securities Act to convert it into a device for dragging local controversies into the federal courts.

---

[9] The Court of Appeals took the process by steps. It admitted that the "sales were apparently by oral communication" yet in the same sentence continued "but the transactions were consummated by the use of the mails" followed by the statement that "Delivery of the deeds and contracts is an integral part of the sale" (R. 87). The application of the words "consummation" and "integral" to an incidental use of the mails after the "sales" admittedly made "by oral communication" is to say the least not self-evident construction.

[10] Indeed, Section 22(a) upon which plaintiffs here base jurisdiction, contains a provision authorizing suit in the state courts and prohibiting removal of such actions to the federal courts (See Appendix).

CONCLUSION

For the foregoing reasons this petition for a writ of certiorari should be granted.

Respectfully submitted,

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October, 1953.

APPENDIX

Section 22(a) of the Securities Act of 1933 (15 U. S. C. § 77v(a) reads as follows:

"Sec. 22. (a) The district courts of the United States, the United States courts of any Territory, and the Supreme Court of the District of Columbia shall have jurisdiction of offenses and violations under this title and under the rules and regulations promulgated by the Commission in respect thereto, and, concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title. Any such suit or action may be brought in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 128 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 225 and 347). No case arising under this title and brought in any State court of competent jurisdiction shall be removed to any court of the United States. No costs shall be assessed for or against the Commission in any proceeding under this title brought by or against it in the Supreme Court or such other courts."

Section 2(1) of the Securities Act (15 U. S. C. §77b(1)) reads as follows:

"Sec. 2. When used in this title, unless the context otherwise requires—

(1) The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a 'security,' or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

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Supreme Court of the United States

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., *et al.*,
Petitioners,

vs.

EMERY C. BLACKWELL, *et al.*,
Respondents.

RESPONDENTS BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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QUESTION PRESENTED

Petitioners concede for purposes of their petition, that the respondents pleadings are sufficient to allege the sale of an "investment contract" as that term is defined by the Securities Act, and rely solely on the proposition that the complaint does not allege a sufficient use of the mails to constitute a violation of Sec. 12 (2) of the Act.

STATEMENT OF FACTS

The statement of fact made by petitioners is partially correct. However, they do not state the transactions concerning the care contracts with accuracy. In most of the sales, the care contracts were dated from two to four weeks after the sales contracts, warranty deeds, notes and deeds of trust. (R. 8, 10, 11, 13, 14, 16, 43). The reason for this was that at the time of the sales, the land was not planted to citrus trees, and while the purchasers were induced to sign a management contract at that time, all of the blank spaces were left blank until a later date because the obligation to pay for care could not begin until the trees had been planted. This meant that the sales were not really completed until some time after the purchasers had returned to their homes in other parts of the State, the Development Company had planted the trees, and the Management Company had a beginning date for their operation.

When this was determined, the Management Company then filled in the blank contract (R. 46-53) and delivered it by mail to the purchasers.[1] The petit-

[1] Petitioners have taken the oral depositions of six of the respondents and it has been established that the Management Contract were completed as above stated and also that statements for work done under the Management Contracts, and payments by the Purchasers were forwarded through the U. S. Mails.

ioners assertion that the transactions were completely entered into and all agreements made and concluded by face to face personal discussions in Hidalgo County, Texas, is not a correct statement.

We further wish to point out to the Court that subsequent to the original purchases, respondents continued to make a continuing investment in the property through their payment for the management or care service. (R. 4, 19, 22-23). The Management Company, to induce this continuing investment sent monthly statements and reports to the respondents through the United States Mails, and it is alleged that these reports contained false and fraudulent statements.

REASONS FOR DENYING THE WRIT

1. The point involved in this suit is of great importance to investors attempting to recover their losses caused by misrepresentation and fraud in the sale of securities. In order that this Court may decide the point in accordance with the intention of Congress we believe that it is of the utmost importance that the facts be fully developed in the trial court.

As we pointed out in our statement of the case, the date of the Warranty Deed and Sales Contracts, was in most of the cases different from the date of the Management Contract. In addition, it is alleged in the complaint that continuing misrepresentations were made to the respondents through the United States Mails, in the form of false statements of work and materials being used in connection with the Citrus Groves, for the purpose of inducing respondents to continue forwarding their money (also through

APPENDIX

77q. Fraudulent interstate transactions.

(a) It shall be unlawful for any person in the sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly —

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

(b) It shall be unlawful for any person, by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, to publish, give publicity to, or circulate any notice, circular, advertisement, newspaper, article, letter, investment service, or communication which, though not purporting to offer a security for sale, describes such security for a consideration received or to be received, directly or indirectly, from an issuer, underwriter, or dealer, without fully disclosing the receipt, whether past or prospective, of such consideration and the amount thereof.

(c) The exemptions provided in section 77c of this title shall not apply to the provisions of this section. May 27, 1933, c. 38, Title I, 17, 48 Stat. 84.

I, Garland F. Smith, hereby certify that on this 25th day of November, 1953, I did mail by prepaid U. S. Mail at Weslaco, Texas, copies of the foregoing brief to counsel for Petitioners, properly addressed.

Garland F. Smith

Garland F. Smith
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Supreme Court of The United States

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., *et al.*,
Petitioners,

EMERY C. BLACKWELL, *et al.*,
Respondents.

RESPONDENTS BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

TO THE HONORABLE, THE CHIEF JUSTICE OF THE UNITED STATES, AND TO THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Come now the respondents, Emery C. Blackwell, Boyd Construction Company, Claude E. Blackwell, Clyde W. Weatherly, Arie K. Smith, Dudley Smith, W. H. Ham, Herbert Clark and Frank L. Danner, and respectfully present their brief in opposition to the petition for writ of certiorari.

OPINIONS BELOW

The trial court sustained petitioners motion to dismiss for lack of jurisdiction on two points. First, that respondents failed to plead the sale of an "investment contract" as defined by the Securities Act of 1933; and Second, that no use of the mails was made sufficient to constitute a violation of Sec. 12(2) of the Act, 15 U.S.C.A. 771(2).

On appeal, the Fifth Circuit reversed and remanded on both points. No evidence has been received, and both the appeal and the petition for certiorari are based solely on the pleadings.

the United States Mails) and increasing the size of their investments. All of these facts will be fully developed on the trial of this case. We do not believe that this Court should be required to decide a question of the importance involved, without having a full development of the facts.

It is true that some of these facts are alleged in a general manner, but the petitioners are fully on notice of what they will need to meet on the trial, and we say that this manner of pleading is contemplated by the Federal Rules of Civil Procedure. In any event, a full presentation of the facts involved will result in the point being decided fairly to all concerned.

2. Petitioners stress in their argument that the present case is local in nature. While it is true that the respondents all reside within the State of Texas, the local nature of this transaction does not involve next door neighbors as petitioners would have this Court believe. Four of the purchasers live approximately 900 miles from their investment, two of them approximately 600 miles, one was an engineer from Wisconsin who moved to Texas after the purchase, with the nearest purchaser residing at least 400 miles from the scene of this operation.[2]

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[2] Judge Allred referred (R. 57) to five similar cases filed against the same principal Defendants and stated that they were grounded on practically the same allegations of conspiracy and fraud. In fact, the cases did not involve the Securities Act of 1933, but were based on the common law and statute of the State of Texas. It is worthy of note as to the extensive nature of the operations of the principal defendants that the 5 plaintiffs in the five consolidated cases were from 5 different states, California, Iowa, Ohio, Indiana and Minnesota.

Alarm is expressed by petitioners, that if the decision below is allowed to stand that the overworked Federal District Courts will be flooded by local land fraud suits. We agree that all of our District Judges are greatly overworked and evidence of this is the fact that the present suit was filed in June, 1951 and the memorandum opinion of the trial court was not filed until April of 1952, some 10 months later. However, there is no basis for the argument that the Federal Courts will be flooded by local land fraud suits. The decision of this Court in S.E.C. v. W. J. Howey Company, 328 U. S. 293, has been on the books seven years, and the decision in Schillner v. H. Vaughan Clarke & Co., 134 F. 2d 875 (C. A. 2, 1943) for 10 years, and the predicted flood of suits has not as yet developed. It is equally open to speculation that the correct decision stopped the fraudulent operators rather than started a flood of litagation.

3. Petitioners point out that the purpose of the Securities Act was to remedy the ineffective relief available to purchasers of securities who were being fleeced by unscrupulous operators. Congress, in the Securities Act of 1933 enacted a very comprehensive statute providing for both civil and criminal liability. The section involved here covers civil liability and is section 12 (2). The comparable section involving criminal liability is 17 (a). The court rulings involving the jurisdictional language under 17 (a) have not required that the misrepresentations

or half-truths be transmitted through the mails.[3]

Therefore, if sec. 12 (2) is restricted to the narrow view of Kemper v. Lohnes 173 F (2) 44, then it is possible that a sale might be in violation of the criminal section and yet the purchaser would have no civil remedy under sec. 12 (2). Sec. 12 (2) is unquestionably a remedial provision and, as such, is entitled to liberal construction. This was recognized by the Court in Schillner v. H. Vaughan Clarke & Co., 134 F. (2) 875 at 877:

"We do not think that this is the inevitable, or even the most natural, meaning of the statutory language. Liability to repay the consideration received is imposed upon any person who 'sells a security ***** by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication' of the untrue or misleading character described in the section. To accept appellant's construction would render the phrase 'oral communication' of most limited application because the section would then reach only interstate telephone calls or conversations where the parties might

[3] The following are examples of mailings which have been held sufficient:

Mailings by Defendants' Agents to the Defendants containing reports of the success of meetings held to obtain money from victims, and remitting cash statements and bank drafts, U. S. vs. Monjar, 47 Federal Supplement 421 Aff'd, 147 Federal 2nd, (C. A. 3, 1944) cert.

Delivery by Mail of a stock certificate after the contract of Sale was concluded orally and the stock paid for. S.E.C. vs. Wimer 75 Federal Supplement 955.

Mailings of Warranty Deeds between Defendants, and to the County Clerk for recording and subsequent delivery to the investors. Mansfield vs. U. S. 155 Federal 2nd 952 (C. A. 5, 1946) cert. denied, 329 U. S. 792, 1946.

be talking across a state line. It would seem much more likely that Congress intended to make the statute applicable if one sells a security by use of the mails, even though the seller's untrue or misleading statement is communicated orally and intrastate."

We have alleged, and will show on the trial that the plan and scheme involved in the sale of the citrus groves and management contracts, was dependent on the use of the United States Mails, and that without the facilities provided by the mails, none of the sales could have been completed. The management contracts were completed and delivered to the purchasers through the mails after they returned to their homes in distant parts of Texas. The Management Contracts are an integral part of the investment, and the sales were not completed in face to face negotiations as stated by petitioners.[4] The instant transactions are the type transactions at which Congress was aiming, and the opinion of the Circuit Court below is in keeping with the intention of Congress.

For the above reasons, the Petition should be denied.

Respectfully submitted,

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[4] Petitioners further argue that the Federal Court should not take jurisdiction of this case because the local courts are fully able to grant relief, and that Sec. 22 (a) prohibits removal of such actions to the Federal Courts. We respectfully submit that unless there has been a use of the mails sufficient to constitute a violation of Sec. 12 (2), the local courts would have no more jurisdiction than the Federal Courts.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., ET AL., *Petitioners,*

v.

EMERY C. BLACKWELL, ET AL., *Respondents.*

PETITIONERS' REPLY BRIEF IN SUPPORT OF PETITION

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1. The SEC in its memorandum has clearly conceded both the conflict between the Circuits in the present case and the importance of this question.

2. Respondents likewise have conceded that "the point involved in this suit is of great importance . . ." (Opposition Memo, p. 3).

3. The only point made by respondents in opposition is that the question presented is of such importance that it should not be decided on the pleadings but only after trial. But no trial is necessary, the issue of law being clearly presented on the face of the complaint. That issue is whether a civil action under the Securities Act of 1933 may

be brought where a sale is completed without use of the mails or interstate commerce, but the securities are delivered by mail after the sale. The Securities and Exchange Commission made no suggestion that additional evidence would be necessary to clarify the question. Nor did the Court of Appeals. The issue is the same admittedly decided to the contrary by the Seventh Circuit in *Kemper* v. *Lohnes*, 173 F. 2d 44. (Opposition Memo, p. 6.)

4. The argument that certain facts developed on deposition might alter the Court's conclusion is without foundation. Those facts appear from the complaint itself.[1]

5. The fact that the mails were used to collect subsequent payments for care of the trees also appears in the complaint. The court below apparently regarded it as too remote in time to have any connection with the sale of the alleged investment contract. But if these mailings have any relevance they are fully alleged in the complaint and can be availed of in this Court. No testimony is necessary to determine the legal question.

6. Since the legal issue is clear from the complaint and no testimony whatsoever is necessary to clarify it, it is an unconscionable suggestion that the District Court should be required to go through an extensive trial. The trial would be devoted primarily to the question of fact concerning whether certain representations were made and whether they were true or false. Such a trial would be unnecessary

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[1] For example, the fact that dates inserted in management contracts were subsequent to the dates of the deeds to the property appears clearly in the complaint. This, of course, resulted from the circumstance that care for the trees was not needed until the trees were planted. The facts are that all the arrangements for the sale of the property, for the planting of the trees and for their care were made in face-to-face conversations in the State of Texas and that mere mechanical and ministerial acts took place thereafter, such as the recording of the deeds, the filing in of the blanks in the management contracts, and the mailing of both documents to the purchasers. This, both the District Court and the Court of Appeals understood in arriving at their respective conclusions.

if this Court should rule that as a matter of law no jurisdiction exists in the federal court.

7. The issue is clear now. It is ripe for decision and the decision is concededly important. Delay is unnecessary and would result in lengthy and expensive litigation which might otherwise be avoided.

8. As to the merits, we have set forth in our petition the reasons why the Congress did not intend to exercise the full limit of its constitutional power. Both respondent and the SEC urge that it is inconceivable that the civil remedy provisions should be placed on a more limited jurisdictional base than the criminal provisions of the Act. But there is good reason for such a difference. Criminal provisions are applied only when government officials, the SEC, and the Attorney General decide that recourse to the federal courts is appropriate in the public interest. In such cases broadening the area of such discretion cannot be expected to flood the federal courts with purely local matters. On the other hand, a civil action may be commenced by anybody who feels himself aggrieved. For example, the ordinary bond and mortgage, like the ordinary promissory note, is a security under the Securities Act, Section 2(1), 15 USC § 77b(1). Bonds and mortgages are normally recorded and thereafter delivered by mail. Under the decision below, private individuals who might prefer the federal courts could bring disputes involving real estate mortgages into the federal courts under the Securities Act. Surely no such intention should be attributed to the Congress when the language it used plainly indicates the contrary.

CONCLUSION

On the basis of all the memoranda, it is clear that the issue is important; that it involves conflict between two circuits; that it is ripe for decision now; and that the question presented is substantial. The petition should be granted.

Respectfully submitted,

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OCTOBER TERM, 1953

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LLOYD M. BENTSEN, SR., et al., *Petitioners*,

v.

EMERY C. BLACKWELL, et al., *Respondents*.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF FOR PETITIONER

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Supreme Court of the United States

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No. 423

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On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF FOR PETITIONER

OPINIONS BELOW

The memorandum opinion of the District Court (R. 34-46) has not been officially reported. The opinion of the Court of Appeals (R. 50-54) is reported in 203 F. 2d 690.

JURISDICTION

The judgment of the Court of Appeals was entered on April 27, 1953 (R. 55). Petitions for rehearing were denied on July 27, 1953 (R. 55). The petition for a writ of certiorari was filed in this Court on October 21, 1953 and was granted on December 7, 1953. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254 (1).

QUESTION PRESENTED

This is a local land dispute in which purchasers of citrus land in the Rio Grande Valley of Texas seek to invoke federal jurisdiction by pleading § 12(2) of the Securities Act of 1933, 15 U.S.C. § 77*l*(2). Does this Section apply to a purely intrastate transaction where the sale is completed without the use of the mails or interstate commerce, but some time thereafter the executed documents evidencing the completed transaction are forwarded by mail to the purchasers?

STATUTE INVOLVED

Section 12(2) of the Securities Act of 1933, as amended, 15 U.S.C. § 77*l*(2) reads as follows:

"Any person who—

* * * * *

> sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security."

Section 22(a) of the Act, 15 U.S.C. § 77v(a) provides that the federal district courts shall have jurisdiction

> "concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title".

The full text of Sections 5, 22(a) and Section 2(1) and the relevant portion of Section 2(10) of the Act are to be found in the Appendix to this brief.

STATEMENT OF THE CASE

The present action was filed in the United States District Court for the Southern District of Texas by eight plaintiffs, residents of the State of Texas,[1] against your three petitioners, residents of the State of Texas, and twelve other residents of the same State (R. 1). The controversy relates to the sale of certain citrus land located in Hidalgo County, Texas, in the Rio Grande Valley. The facts are as follows:

The eight plaintiffs purchased the land in question from one of the defendants, Pummill Development Corporation, in 20 and 40 acre parcels, and paid for citrus trees planted or to be planted on their tracts. The price was generally $8,000 for a 20 acre tract plus $2,500 for the trees planted or to be planted on the tract (e.g. R. 5, 6, 7).[2] Most of the purchasers also entered into contracts with another of the defendant companies, Pummill Management Company, which agreed to take care of the trees in question for a fee of $1 per acre per month and the cost of labor and material expended (R. 3, 5, 6, 7, 8, 9, 10). The purchasers under their care contracts agreed to set up and did set up a fund in a local bank to be drawn on by Pummill Management Company. As the money was expended, Pummill Management Company forwarded by mail monthly a statement of

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[1] One other Texas resident intervened as plaintiff (R. 26-28).

[2] One couple obtained the 20 acre tract for $7200 (R. 5-6).

the expenditures made on the purchasers tract. Under the care contract the owner was then obligated to replenish the bank deposit (R. 30).

The complaint alleged that the land in question was part of a block of 800 acres offered to persons resident "outside of the Rio Grande Valley of Texas", "together with a property management or care contract, the whole transaction being treated as an investment by both buyer and seller." (R. 2). It was then alleged that the transactions were induced by false representations of some of the individual defendants (R. 14, Par. VII, 3), and that the other defendants in various manners aided the said defendants (R. 13, et seq., Par. VII).[3]

Plaintiffs alleged that the sale of the land coupled with the agreement to care for the land made the transaction the sale of an investment contract and therefore of a security under the Securities Act (R. 2). The decision of this Court in *Securities and Exchange Commission* v. *W. J. Howey Co.*, 328 U.S. 293, was relied on (R. 3).

The use of the mails was alleged in the following manner:

The purchase of the land was in each case made on a personal visit of the purchaser to the property in Hidalgo County, Texas,[4] and payment was made at the time. In some cases the payment was all in cash (R. 3, 9, 27) and in others by cash and notes (R. 5, 6, 7, 7-8, 8).[5] Deeds to the land were executed the same day and recorded in

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[3] In the case of your petitioners it is alleged that their participation consisted in the fact that they had been the former owners of the property and had a vendor's lien on the property (R. 13, 14, Par. VII, 1). This is accompanied by allegations that the vendor's lien was "fraudulent" and that by this means the petitioners were participating in "spoils and plunder." The other defendants are counsel who organized the land selling company, the secretary of the caretaking company, various brokers, and a bus driver for the land company (R. 13-15).

[4] E.g., as to four of the plaintiffs, it was alleged that they were induced by one of the broker defendants to make a trip from their homes in another part of Texas to the Rio Grande Valley (R. 15, paragraph 8).

[5] One purchaser traded some other land in Pecos, Texas, in part payment (R. 4).

the purchaser's name (R. 4, 5, 6, 6-7, 7-8, 8-9, 9-10). Generally on the same day that the plaintiffs purchased the land from the Development Company, Pummill Management Company "executed and delivered to the said Plaintiff a care contract", agreeing to care for the property on the terms stated above (R. 28, 5, 6, 7, 8, 9, 10). *The transactions were thus completely entered into and all agreements made and concluded by face to face personal discussions in Hidalgo County, Texas, without use of the mails or any means of interstate commerce. This included the purchase of the land, the deeding of the property and the execution of the care contract. No allegation or contention to the contrary is made.*

In each case, however, it is alleged that the warranty deed to the property and the care contracts as well, were at a later date forwarded to the plaintiffs at their residences through the mail.

This is the sole basis of jurisdiction claimed and considered by the court below. In the language of the complaint, it was only "after" the oral representations complained of had been made and after the contracts had been entered into for the purchase of the land and care of the trees, that the mails were used to deliver copies of the documents previously executed (R. 11-12).[6]

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[6] Although this does not appear clearly from the complaint, it was argued by respondents in their opposition to the Petition for Certiorari and is conceded that the occasion for the use of the mails was as follows:

The deeds that were executed on the same day were presented for recordation in the appropriate county office in Hidalgo, Texas. After being recorded, the deed with notice of recordation was mailed to the purchaser at his home.

As to the care contract, that was executed at the time of the purchase of the land, but since the land was not in most cases planted to citrus trees and the monthly $1 an acre fee for care of the trees under the care contract as well as the expenses of such care would not commence until the trees were planted (R. 30), the executed contract was left with a blank space for the date when the trees would be planted and the obligation of care actually begin. This took in each case several weeks. The blank in the previously executed contract was then filled in by Pummill Management Company and the mails were used to send the contract to the purchaser.

The Rulings Below

The District Court (Allred, J.) dismissed the complaint, stating:

> "It is clear that plaintiffs have framed their complaint with an eye to S.E.C. v. W. J. Howey Co., et al., 328 U.S. 293. In the words of counsel for defendant, Pummill: 'These residents of Texas, having read some cases and being anxious to secure Federal jurisdiction for trial of land fraud suits have plead in a manner calculated to obtain Federal jurisdiction.' Plaintiffs almost succeed in doing this; but, for reasons hereafter set out, I hold they have not." (R. 38)

After holding that no sale of a security was alleged (R. 38-41), Judge Allred also ruled that the use of the mails was insufficient, since the alleged false statements were not made by use of the mails, and the only use of the mails was for delivery after sale (R. 41-45). He relied on and quoted extensively from *Kemper* v. *Lohnes*, 173 F. 2d 44 (CA 7 1949).

On appeal, the Court of Appeals for the Fifth Circuit reversed on both points. It held that the complaint adequately alleged that a security was involved (except in the case of two of the plaintiffs who may not have executed care contracts) (R. 53, 54). It also said that the use of the mails to deliver the "deeds and management contracts" was sufficient to bring the transaction within Section 12(2) of the Act (R. 54).

Certiorari was taken here limited to the question of the construction of Section 12(2) of the Securities Act. Petitioners specifically stated in the petition that they believed that the Court of Appeals erred also in holding that the sales of land in question were investment contracts and therefore securities. However, in the context in which the matter came to this Court on the complaint alone, the question was merely one of construction of the pleadings not meriting review by this Court under its stated

standards. The petition as granted was accordingly limited to the question of Section 12(2).[7]

SUMMARY OF ARGUMENT

I

Section 12(2) of the Securities Act gives a civil remedy of rescission or damages only against one who "sells" a security "by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication" which is false or misleading. In the present case no allegation is made that any means of interstate commerce were used or that a prospectus was used. The transaction was a local real estate transaction concluded face to face in which the mails were used only to deliver documents *after* the sale was concluded.

It cannot be held that the securities were sold "by the use of the mails" within the meaning of the statute. The sole use of the mails was for delivery of the documents constituting the alleged security *after* sale. The concept of delivery after sale is distinct from the concept of sale. In other sections of the statute relating to the registration of securities with the Securities and Exchange Commission, the Congress made this clear by applying those provisions of the Act to the use of interstate commerce or the mails both "for the purpose of sale or for delivery after

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[7] If it should be necessary after action by this Court, petitioners will present to the trial court, evidence to establish that no security sale was involved.

For example, at trial, it would be established, among other things, that the allegation that the land was to be planted to "citrus" conceals the fact that each purchaser made his own managerial judgment, and had various percentages of grapefruit, valencia oranges and even tangerines planted on his land. These and other facts which have already been admitted on depositions, will, we believe, clearly establish that there is no basis for the allegation that a security is involved in these transactions, and that they are in fact ordinary land transactions. We trust, of course, that a ruling of this Court on the issue presented by this petition will make such a trial unnecessary.

sale". The failure so to provide in Section 12(2) is a clear indication that Congress intended the section to apply only to a sale and not to a delivery after sale. This, of course, disposes of the matter.

In addition, the security was not sold "by the use of the mails" "by means of" the prior face to face oral communication. The statute does not apply to a transaction completed face to face within a state. The terms of the statute make it clear that a civil remedy applies where the security is sold by a written false communication, i.e., a prospectus, transmitted in interstate commerce or through the mails, or where the sale is made by false oral communications by interstate telephone. The language of the statute does not permit liability in other circumstances.

There is no necessity for construing the civil liability section in the same way as the criminal sections of the statute since the criminal sections are differently and perhaps more broadly phrased. In any event the criminal sections have never been construed by this Court to apply as broadly as the court below applied the present civil section.

II

All the parties on both sides are residents of the State of Texas. The real estate involved is situated in Texas. The State of Texas provides adequate laws and courts to protect its citizens against fraud in local transactions. The Texas Blue Sky law has an identical definition of "security" to that contained in the federal Act and a civil relief section. The common law grants adequate relief if the transactions are held not to be securities but merely real estate sales. Evidence to this effect is at hand in earlier actions with substantially identical allegations commenced against petitioners by respondents' counsel. In those actions reliance was placed upon state and not federal law, federal jurisdiction being there established by diversity. The protection of investors will not be furthered by extending a forum in the federal court to plaintiffs in local real

estate transactions in addition to their completely adequate local remedy.

III

Extending federal jurisdiction to cover this case will require the federal courts to entertain a great number of actions of an essentially local nature. The statutory definition of security is broad, as the ruling below shows. Mortgage bonds on homes are also securities. So are promissory notes. Under the decision below, local controversies could flood the federal courts. And no restraint by any government agency is available in the case of civil actions.

IV

No congressional purpose in enacting the Securities Act would be furthered by the construction of the court below. The basic assumption of that construction is that Congress meant to exert its power to the full constitutional extent permitted. There is no basis for this assumption in the legislative history or the purposes of the statute. The legislative history shows an affirmative intention to exclude local transactions from the scope of the Act. It shows a specific understanding by the Congress that state Blue Sky laws adequately covered local transactions. It shows an intention that the Securities Act shall cover only transactions of an interstate or national character. The Congress expressly stated that it did not wish to extend the statute "beyond the need of public protection."

ARGUMENT

I. The Statutory Language Cannot Apply to the Facts Pleaded Here

The language of the statute is clear. Section 12(2) provides that an action shall lie to recover the consideration paid or for damages against any person who "sells a

security . . . by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication" which is false or misleading. Some of the defendants sold real estate to the plaintiffs and other defendants entered into contracts to care for that real estate. The Court below decided (contrary to what we believe to be correct, see pp. 6, 7, *supra*) that these arrangements constituted "securities" under the broad phrase "investment contract" in the definition contained in the Securities Act of 1933 (§ 2(1)). But the complaint here does not allege facts showing that the "securities" in question were sold "by the use of any means or instruments of transportation or communication in interstate commerce or of the mails". For, accepting the allegations of the complaint, the sales involved were completed before use of the mails, and the mails were used only for delivery after sale. *A fortiori* the sale was not made "by use of" interstate commerce or the mails "by means of" a prospectus or oral communication which is false or misleading. There is no allegation whatsoever that means or instruments of transportation or communication in interstate commerce were used. There is also no claim that a prospectus was employed or required. Compliance with the statute is sought to be based solely on "use of the mails" for delivery of securities after sale, and on *prior* "oral communication" involving neither the use of the mails nor interstate commerce. This does not meet the test of the statute which requires that the sale be made *by use of* the mails *by means of* a false or misleading communication.

(1) The securities were not sold *"by the use of the mails"* as required.

The facts pleaded are merely that the plaintiffs and certain of the defendants entered into face to face transactions in Hidalgo County, Texas; that as a result of those

transactions the defendant Pummill Development Company sold the plaintiffs certain real estate and trees to be planted thereon; that the defendant Pummill Management Company agreed to care for the trees. *The contracts of sale of real estate and for the care of the trees were entered into face to face in Hidalgo County, Texas. The sales were thus completed without use of the mails or interstate commerce in any way.* It was only, as the complaint alleges (¶ V, R. 11, 12), "after" the sale that the mails were used to deliver the recorded deeds and the completed contracts to the purchasers as their evidence of the transaction which had been previously concluded. On these facts, the sales cannot properly be said to have been made "by the use . . . of the mails".

The use of the mails was not "to sell" the security as required. It was to transmit evidence of a previously completed sale. The concept of "delivery after sale" is distinct and different from the concept of "sale". It is something that occurs not as a part of the sale but "after" the sale.

The Congress understood this difference and when it intended to apply the Act to delivery of securities after sale, it said so. Thus in Section 5 of the Act dealing with the necessity for registration of new public issues of securities with the Securities and Exchange Commission, registration is required where the facilities of interstate commerce or the mails are used to carry securities *"for the purpose of sale or for delivery after sale . . ."* See Section 5(a)(2), 15 USC § 77e(a)(2). See also § 5(b)(2), 15 USC §77e (b)(2). The specific reference to "delivery after sale" in Section 5 and its failure so to provide in Section 12(2) clearly establishes that Section 12(2) cannot be read to include delivery after sale. The language of Section 5 establishes that "delivery after sale" is something different from and subsequent to the sale itself and not covered by

Section 12(2) which deals only with *sale* by use of the mails.[8]

This being so, the Section does not apply and the complaint must fail, without more. However, we shall also establish that the complaint fails to meet the statute in another respect.

(2) The securities were not sold *"by the use of the mails, by means of a prospectus or oral communication"* as required.

Plaintiffs contend that certain defendants sold the "securities" here involved "by the use of the mails [i.e., the delivery of the security after sale], by means of a[n] . . . oral communication (the face to face oral communications made in the process of negotiating the sale but before the use of the mails) . . ." The idea that the facts pleaded may be properly so described involves a complete distortion of the ordinary meaning of language.

We can present no clearer analysis than did the Seventh Circuit in *Kemper* v. *Lohnes*, 173 F. 2d 44, 45 (1949), as follows (quoted by the District Court R. 43-44):

> "The phraseology of the section as applied to pertinent allegations of the complaint may be reduced to read that any person who 'sells a security . . . by the use . . . of the mails, by means of . . . oral communication . . .' This must be so because it is not claimed that

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[8] The definition of sale also clearly excludes the concept of delivery. Section 2(3) of the Act states that the terms " 'sale', 'sell', 'offer to sell', or 'offer for sale' shall include every contract of sale or disposition of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value;" 15 USC § 77b(3). The Second Circuit in *Schillner* v. *H. Vaughan Clarke*, 134 F. 2d 875, at 877, stated, that a delivery of a security was a "disposition" of a security. This is incorrect. Note the facts in the present case. The real estate here was deeded to the purchasers on the date they entered into the contract of purchase and was then recorded in the purchaser's name in the local court. All rights were vested at this time. No rights were disposed of or acquired as a result of the subsequent mailing of the deed. The care contracts likewise represented an obligation fully entered into by the parties face to face. That obligation was neither increased nor diminished by sending evidence of the agreement to the plaintiffs through the mail several weeks later.

'any means or instruments of transportation or communication in interstate commerce' was used other than that of the mails, nor is it claimed that there was any untrue statement 'by means of a prospectus.' The untrue statement, as alleged, was by means of an 'oral communication.' Of course, it is evident that an untrue statement made by 'oral communication' cannot take place through the mails, which we think indicates that the section does not contemplate the inclusion of an 'oral communication' in connection with 'use of the mails.' "

"Now to approach the matter from another angle. Assuming that an 'untrue statement' is the gravamen of the cause, as we think it is . . . such untrue statement must be made either (1) 'by means of a prospectus' or (2) by 'oral communication,' and in turn these two means of imparting an untrue statement must be made (1) 'by the use of any means or instruments of transportation or communication in interstate commerce' or (2) 'by the use . . . of the mails.' It appears to us, in fact we think it unreasonable to think otherwise, that 'by the use . . . of the mails' was employed solely in connection with 'by means of a prospectus', as the latter term is defined in the Act. Sec. 77b(10) states: 'The term "prospectus" means any prospectus, notice, circular, advertisement, letter, or communication, written or by radio . . .' Thus the matters included in this definition are written and such as are commonly sent through the mails. An oral communication cannot be sent through the mails, and it is unrealistic to associate such a communication with the use of the mails.

"Of course, the phrase 'oral communication' must be recognized and given a place in construing the section, but that may be done by associating the term with a means of 'communication in interstate commerce'. Sec. 77b(7) states: 'The term "interstate commerce" means trade or commerce in securities or any transportation or communication relating thereto among the several States . . .' This certainly would include telephone conversations as means of communication in interstate commerce . . ."

In *Schillner* v. *H. Vaughan Clarke*, 134 F. 2d 875, 877 the Second Circuit adopted a contrary view because, in part at least, it believed it unreasonable to construe the term "oral communication" to "reach only interstate telephone calls". But it is by no means unreasonable so to limit the application of the phrase "oral communication". Securities sales in interstate commerce at which the Act was directed, are conducted by three major normal means of communication: (a) the interstate mails; (b) the interstate telephone (*Cf. Murphy* v. *Cady*, 30 F. Supp. 466 (D. Me. 1939)); and (c) the interstate telegram.[9] The phrase "prospectus or oral communication" covers all three normal methods of communication. "Prospectus" covers two and "oral communication" the other. Certainly this is a reasonable and natural way of treating the two phases of the problem—the written and the oral communication—in a statute of a national government dealing with interstate commerce. To apply the phrase "oral communication" to a *face to face* conversation, as the Court in *Schillner* did, is to construe the statute as though it were adopted by a local government rather than a federal government under a delegated power over interstate commerce.

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It has also been argued in the courts below that Section 12(2) must be construed as broadly as certain other provisions of the securities laws, e.g., Section 17(a) of the Securities Act of 1933, making fraud and false statements unlawful, and Section 10(b) of the Securities Exchange Act of 1934. It should perhaps be sufficient to say that the language of those provisions is quite different from that of Section 12(2). (See the opinion of the District Court R. 45). Had Congress intended the same result in both cases, it could easily have used the same language. It is therefore

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[9] See the statement of Rep. Greenwood, 77 Cong. Rec. 2914: "All lines of publicity, whether by use of the mails, the telegraph, the telephone, radio, prospectuses or any other form of publicity that will lead an investor to purchase securities have been covered by the bill."

The Act includes radio with the written rather than the oral communications. See the definition of prospectus (Section 2(10)) in the quotation from the *Kemper* case, *supra* p. 13.

unnecessary to consider whether there may be reasons for construing those statutes more broadly.[10] Further, this Court has never decided that, under these differently phrased provisions, federal jurisdiction is invoked by a use of the mails to deliver a security after the entire transaction of sale has been completed otherwise. Indeed, even under the all inclusive mail frauds statute, there comes a point where a transaction complained of is completed and use of the mails thereafter no longer has any relation to the objective of the statute. Cf. *Kann* v. *United States*, 323 U.S. 88.[11]

II. Investors Will be Adequately Protected Under the Petitioner's Construction of the Statute

No issue of protection of investors is involved. To refuse jurisdiction here would merely remit the investor to a clearly adequate remedy under state law. If the land sales and care contracts are indeed securities under the definition of the Securities Act of 1933, they will in all likelihood also be so held under the identical definition of the Texas Blue Sky Law (Texas Revised Statutes 600a § 1(a)). Plaintiffs could, in that event, enforce liability for misrepresentation in any competent court of the State of Texas under the civil liabilities provision of that law (id. § 33a).[12] If the

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[10] See pp. 17, 18, *infra*.

[11] There was some argument in the respondents' brief in opposition to the effect that the statements of expenditures for the care of the trees which were delivered monthly after care had commenced (thus commencing at least two months after the "sale" in question) had some relevancy to the application of the Securities Act. The court below did not rely on these mailings, apparently regarding them as too remote from the sale and limiting its ruling to the "delivery of the deeds and [care] contracts" (R. 54). Plainly, if the real estate and care arrangements represented a security, that security was sold when the contracts were entered into. The care statements were merely a report of actual expenditures which, under the care contract, obligated the purchasers to replenish their deposits in the local bank in Hidalgo County, Texas (R. 30). They were not prospectuses, a prospectus being defined in the Act as a writing "which offers any security for sale" § 2(10). Plainly, the "securities", if such they were, were not offered or sold by means of these statements of amounts expended for care, and no jurisdiction under Section 12(2) arises from the mailing of these statements of expenditure.

[12] See Loss, Securities Regulation, pp. 962-982, for a discussion of the civil liabilities provisions of various Blue Sky laws with frequent reference to Texas.

transactions are not securities transactions but, as we believe, simple real estate sales, the Texas law on rescission for false statements or fraud and deceit is surely adequate.[13]

Certainly under the differing remedies provided by state law and by Section 12(2), the plaintiffs rights may vary somewhat. But in general the state court remedies will give substantially equivalent relief. This is objectively established here by the fact, noted in the opinion on the district court (R. 37 n. 4), that where the same counsel in a similar litigation against the same defendants, represented out of state plaintiffs, they sued in the federal court only on diversity of citizenship. In that case, they relied on Texas common law and made no mention of the Securities Act.

Accordingly no reason related to the protection of investors exists for extending federal jurisdiction to purchasers in local real estate transactions such as the present one. The remedies under state law are adequate.

III. To Sustain the Ruling Below Will Extend Federal Jurisdiction to a Host of Cases Having No Relation to the Objective of the Securities Act

The definition of "security" in the Securities Act of 1933 is in the most inclusive terms. It specifies as a security for example "any note, . . . evidence of indebtedness, . . . investment contract" besides the usual "stock," "bond, debenture, etc." The present case shows some of its scope as applied to real estate transactions.[14] The Ninth Circuit has recently held that the Act applies to a simple promissory note. *Llanos* v. *United States*, 206 F. 2d 852 (Sept. 4,

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[13] The relative advantages and disadvantages from the plaintiff's point of view of an action under Section 12(2) and under the common law are considered in Loss, *op. cit., supra*, at pp. 997-1001.

[14] We should perhaps also mention its application to the animal world. *S.E.C.* v. *Payne*, 35 F. Supp. 873 (SDNY 1940) (silver foxes); *Hollywood State Bank* v. *Wilde*, 70 Cal. App. 2d 103, 160 P. 2d 846 (1945) (chinchillas); *Stevens* v. *Liberty Packing Corp.*, 111 N.J. Eq. 61, 161 Atl. 193 (1932) (rabbits).

1953). The purchase of a dwelling house is almost invariably accompanied by the execution of a bond and mortgage which is plainly an "evidence of indebtedness".

The ruling below would require the federal courts to open their doors to private litigants who claimed that false or misleading oral statements were made to them before they agreed to advance the mortgage money. For in the normal case the bond and mortgage will be recorded and delivered by mail. Similarly under that ruling, holders of promissory notes of their neighbors could not be barred from the federal courts on claims of oral misrepresentations e.g. of financial standing, provided the promissory note was dropped in the mail. In such cases also the debtor could be pursued by federal court process throughout the United States, if he had moved away from the place where the "sale" of the "security" took place. And all this without even any limitation as to jurisdictional amount or diversity of citizenship. *Deckert* v. *Independence Shares Corporation*, 311 U.S. 282.

Plainly the Congress in the Securities Act of 1933 intended no such mares nest for the overburdened federal judiciary.[18] The state courts are available and adequately equipped to deal with such local transactions.

The broad definitions and extended scope of the Act may serve a purpose where the governmental discretion of the Securities and Exchange Commission or the Attorney General may choose the case for litigation on the basis of public

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[18] Judge Allred referred (R. 45) to "the pressure of constant trial work for the past three months" and noted (R. 37, n. 4):

> "In five similar cases filed against the same principal defendants here, (in which jurisdiction was grounded on diversity of citizenship), practically the same allegations of conspiracy and fraud were made. After a jury trial lasting nearly four weeks, there were findings of no conspiracy and a hung jury on the issue of fraud by the selling company."

The condition of the dockets in the other federal courts needs no elaboration. See ANNUAL REPORT OF DIRECTOR OF ADMINISTRATIVE OFFICE OF THE FEDERAL COURTS TO THE JUDICIAL CONFERENCE OF THE UNITED STATES, SEPTEMBER 1953, particularly the summary at page 1 entitled "The Still Unmet Need for More Judges."

interest.[16] But here a right was given a private litigant to pursue at his own pleasure unlimited by governmental or court restraint. We believe the Congress wisely limited that right to a showing of grounds of jurisdiction which gave substantial evidence that the problem was of more than local significance. The Court should not depart from that limitation. To sustain the decision below would run the danger of converting a great statute designed for the protection of investors against interstate securities fraud into a device for choking the federal courts with controversies purely local in nature.

IV. The Congressional Purpose Is Not Served by the Construction Adopted by the Court Below.

Indeed there is no serious argument that the statute on a normal reading would cover the transaction in question or that any substantial purpose would be served by the construction of the court below. Rather it is the contention of those supporting the ruling below that the language used by the Congress was inartistic, that it meant something different from what it said, and that the general policy considerations which occasioned the passage of the Securities Act required a "liberal" construction of the statute to accord with those policy considerations rather than the language the Congress used.[17]

The argument is baseless. There is no legislative history of Section 12(2) itself which helps those who would read the statute more broadly than its terms. The Section

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[16] See Section 20(b) authorizing injunctive proceedings by the Commission "in its discretion" and criminal proceedings by the Attorney General "in his discretion".

[17] *Cf.* Loss, *Securities Regulation*, p. 1062. In agreeing with the construction adopted by the court below the author finds it necessary to preface his position with a statement that "Section 12(2) is not a model of draftsmanship".

But *Cf.* the statement of Rep. Greenwood, 77 Cong. Rec. 2913: "I never have read a bill that appeared to be more carefully drawn, with reference to all of its features and technicalities, than this bill."

appeared substantially in its present form in the bill as reported by the House Committee and no discussion of the specific relation of the section to the use of interstate commerce or the mails appears in the reports or debates. The proponents of the view adopted by the court below are therefore driven to argue from the assumed purposes of the Act in general.

That argument, as stated in the *Schillner* case, *supra,* is that in the Securities Act the Congress "meant to exert its power to the full constitutional extent permitted by the commerce clause and the postal clause" 134 F. 2d at 878. Were this a correct statement of the congressional purpose, there might be reason to distort the language employed by the Congress in an attempt to achieve the assumed objective. But there is no warrant in the legislative history, in the conditions leading to the passage of the Act or in general public policy for such a conclusion. Instead these criteria establish that the Congress in the Securities Act did not intend to "affect transactions beyond the need of public protection" by the federal government (H. Rep. 85, 73d Cong., 1st Sess., p. 7). The purposes of the Congress would be better served by the construction advocated by petitioners here.

Indeed, the approach of *Schillner* and of the court below ignores the basic nature of our federal system. It does not heed the admonition of this Court that "in ascertaining the scope of congressional legislation a due regard for a proper adjustment of the local and national interests in our federal scheme must always be in the background". *FTC* v. *Bunte Bros., Inc.,* 312 U. S. 349, 351. It does not consider that when Congress does see fit to regulate local business "and thereby radically readjusts the balance of state and national authority, those charged with the duty of legislating are reasonably explicit and do not entrust its attainment to that retrospective expansion of meaning which properly deserves the stigma of judicial legislation." *Kirschbaum* v. *Walling,* 316 U. S. 517, 522.

1. *The Law Was Intended Primarily to Deal With the Area of Interstate Commerce Beyond the Power of the States to Control.*

Although the Securities Act of 1933 involved a great extension of the scope of federal regulation, the Congress was not embarking on a field that was unoccupied by the states. It was faced with no necessity, and it expressed no desire, to extend its power to every local transfer of shares well within the regulatory power of the states. Rather in adopting the Securities Act of 1933 the Congress was acting in the best conservative tradition of our federal system. It acted to bring the power of the federal government to bear in the area where the states were powerless to act.

The inapplicability of the Act to transactions like the present was specifically declared on the floor of the House on two occasions. First:

> "Mr. Parker of New York.[18] The law does not affect intrastate business in the least.
>
> Mr. Britten. Of course it does not . . ." 77 Cong. Rec. 2921.

And again:

> "Mr. Cannon [of Wisconsin]. Within the last few months I tried a case in which an influential high officer of a bank obtained from a poor man his life savings by selling to him securities he either knew or, in the exercise of due care, ought to have known were worthless.
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>
> Mr. Mott. Did the transaction of which the gentleman speaks take place entirely within his own State?
>
> Mr. Cannon of Wisconsin. Yes.

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[18] Senior Republican member of the House Committee on Interstate and Foreign Commerce, and a proponent of the bill. The Committee was unanimous in favor of this bill in general, two members dissenting from a provision which was not incorporated in the law as passed. See H. Rep. 85, 73d Cong., 1st Sess.

> Mr. Mott. Is it the gentleman's idea that such a transaction comes within the purview of this legislation?
>
> Mr. Cannon of Wisconsin. Oh, no; I am just citing that as an illustration of the activity of some of our bankers." 77 Cong. Rec. 2941.

These clear statements of intention not to deal with local transactions of the type here involved are mere expressions of the obvious.

It should be remembered that state Blue Sky laws regulating the Securities Act antedated the Securities Act by some twenty years and that when the Securities Act was passed forty-seven of the forty-eight states had such laws. Loss, *Securities Regulation*, pp. 18, 19.[19] These laws had been sustained by this Court under the due process clause. *Hall* v. *Geiger-Jones*, 242 U. S. 539.

The Congress was of course aware of the existence of this state legislation.[20] It specifically provided that it was not usurping this field, and that the rights it gave to investors were "in addition to any and all other rights and remedies" existing under state laws (Section 16) and that "nothing in this title shall affect the jurisdiction" of any State Blue Sky Commission "over any security or any person" (Section 18). Plainly it was not seeking to duplicate state regulation in order to give investors a new forum in the federal courts for grievances already adequately cognizable under state laws.

Rather it built on this foundation of state regulation by adding its own scheme to govern the area which the states could not reach—interstate trade in securities. It sought to "supplement" the blue sky laws of the states and make it "impossible for dealers and underwriters to evade the State laws by the shipment of their securities and prospectuses and other material in interstate commerce or through the

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[19] Nevada was the exception.

[20] See Rep. Mapes, 77 Cong. Rec. 2912: "Of the 48 states in the Union, all but 1 have some sort of blue-sky legislation."

mails". Rep. Mapes, 77 Cong. Rec. 2912. For the Congress was advised that the great national trade in securities was unregulated because it could not be reached by the individual states, and that in this field state regulation needed to be supplemented by a national law. The Hearings before the House Committee on Interstate Commerce were opened by the testimony of Hon. Houston Thompson, as chief spokesman in favor of the bill, with a statement to this effect.[21] Similar statements were made in floor debate.[22]

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[21] At page 10 of the Hearings on H. R. 4314, March 31, 1933, he stated as follows:

> "These 'blue sky' laws of the States have failed, as is very obvious, in meeting the great problem, and that is due to a number of facts, First of all, a lack of unifomity [sic] of laws, and, second, the fact that, on the subject of extradition, those who are putting out securities can sell and send them across the State line into another State without being able to be reached so far as a criminal penalty is concerned. You only extradite and bring a man back after he has fled from a State. Well, nowadays securities can be sold from New York State over into Illinois, and the consummation of the contract can only be terminated by the consent of the seller from New York, and in that way the person in Illinois suffers if the security is not a good one; and yet the wrongful act has been committed outside the State, and there is no way of reaching the person outside of the State."

See also the statement of Robert E. Healy, General Counsel of the Federal Trade Commission, later a Commissioner of the Securities and Exchange Commission. Hearings on S. 875 at 214-215.

[22] See Rep. Wolverton, 77 Cong. Rec. 2931 as follows:

> "The failure to prevent such losses is not due to any lack of stringency in the statutes already enacted by the several States, but, in a large measure, because of the inability of State laws to reach interstate transactions in such securities. Fraudulent securities are largely sold and distributed by agencies of communication which extend beyond state lines. The jurisdiction of State regulatory measures is necessarily confined or limited to transactions within the State. The channels of interstate commerce are open and free from such State regulation and control. Thus securities that may be precluded from sale in an intrastate transaction are immune when the transaction extends beyond the boundaries of that particular State."

Mr. Wolverton was a member of the Committee on Interstate and Foreign Commerce which was in charge of the bill.

See also Rep. Chapman, also a member of the Committee, 77 Cong. Rec. 2935; Rep. Greenwood, 77 Cong. Rec. 2914: "No state has power to control publicity of securities. Some issues come from abroad, some of them are national in character, and no state has such authority or power.".

The Act was a response to a presidential recommendation "for Federal supervision of traffic in investment securities in interstate commerce," and for full disclosure with respect to "every issue of new securities to be sold in interstate commerce". See H. Rep. No. 85, 73d Cong., 1st Sess., pp. 1, 2.[23]

The entire scope of the Act was directed at the problem of interstate sales. Registration under the federal law was required only if interstate commerce was employed in the sale or delivery after sale. But local concerns selling to citizens of their own state were left to local regulation even though they used the mails in the process (Section 5(c) of original Act; Section 3(a)(11) of amended Act).

As the House Committee pointed out, H. Rep. 85, 73d Cong., 1st Sess., p. 7:

> "Section 5(c) also exempts sales within a State of entire issues of local issuers. In view of these exemptions and the restriction of the bill's application to new offerings, the bill does not affect transactions beyond the need of public protection in order to prevent recurrences of demonstrated abuses."

2. *The Purpose and Effect of the Partial Reliance On the Postal Power.*

Since the constitutional scope of the commerce clause of the federal Constitution was not in 1933 as clear as it is today, jurisdiction was buttressed by the alternative provisions relying on the use of the mails, and supplemented by a separability clause (Section 26).[24]

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[23] See this Report (of the House Committee on Interstate and Foreign Commerce reporting the bill favorably to the House,) at p. 3: "Resting upon the power of Congress under the Constitution over interstate and foreign commerce, the bill closes the channels of such commerce to security issues unless and until a full disclosure of the character of such securities has been made". See also Rep. Rayburn, 77 Cong. Rec. 2918. See also, e.g., S. Rept. 47, p. 1, referring to the basic policy to inform the investor concerning "securities to be offered for sale in interstate and foreign commerce"; *id.* p. 2, the statement that the Act requires registration "when a person or corporation is about to sell securities in interstate commerce."

[24] *Cf.* Rep. Beck, 77 Cong. Rec. 2935-2939, particularly the reference (at 2937) to the doctrine of *Paul* v. *Virginia*, 8 Wall. 168.

The constitutional problems surrounding the time of its enactment have left their mark on the Securities Act of 1933. Although the commerce power has now been confirmed in its broadest scope, Section 12(2) would still apply to a purely local transaction where a prospectus was sent through the mails within a single state and was used to sell a security. In such a case the courts would of course be required to apply the Act in accordance with its terms although the basic objectives of the Congress would not be advanced. We suggest no limitation of the language of the Congress in such cases.

But where as here the language rather commands a conclusion that federal jurisdiction does not exist, there is no occasion to extend the language of the statute beyond the objectives of the Congress or "beyond the need of public protection". *Cf.* H. Rep. No. 85, 73d Cong., 1st Sess., p. 7.

CONCLUSION

The language of the statute is plain. It does not create a cause of action in the federal court under the circumstances of a face to face transaction solely within a state. The use of the mails to deliver documents evidencing a previously completed transaction does not bring the matter within the Act. An adequate remedy exists under the law and in the courts of the State of Texas. The decision below unnecessarily extends federal power beyond the purposes intended by the Congress. The decision below would open the federal courts to much local litigation. The judgment of the Court of Appeals should be reversed with directions

to affirm the judgment of the District Court dismissing the complaint.

Respectfully submitted,

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February, 1954

APPENDIX

Section 5 of the Securities Act of 1933 (15 U.S.C. § 77e) reads as follows:

"Sec. 5. (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation any such security for the purpose of sale or for delivery after sale.

(b) It shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security registered under this title, unless such prospectus meets the requirements of section 10; or

(2) to carry or to cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of section 10."

Section 22(a) of the Securities Act of 1933 (15 U.S.C. § 77v(a)) reads as follows:

"Sec. 22. (a) The district courts of the United States, the United States courts of any Territory, and the Supreme Court of the District of Columbia shall have jurisdiction of offenses and violations under this title and under the rules and regulations promulgated by the Commission in respect thereto, and, concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title. Any such suit or action

may be brought in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 128 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 225 and 347). No case arising under this title and brought in any State court of competent jurisdiction shall be removed to any court of the United States. No costs shall be assessed for or against the Commission in any proceeding under this title brought by or against it in the Supreme Court or such other courts."

Section 2(1) of the Securities Act (15 U.S.C. § 77b(1)) reads as follows:

"Sec. 2. When used in this title, unless the context otherwise requires—

(1) The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a 'security,' or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

Section 2(10) of the Securities Act of 1933 (15 U.S.C. § 77b(10)) so far as here relevant provides as follows:

"(10) The term 'prospectus' means any prospectus, notice, circular, advertisement, letter, or communication, written or by radio, which offers any security for sale; . . ."

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HAROLD B. WILLEY, Clerk

Supreme Court of the United States

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN., et al, *Petitioners*
v.
EMERY C. BLACKWELL, et al, *Respondents*

On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF FOR RESPONDENTS

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LLOYD M. BENTSEN., et al, *Petitioners*

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On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF FOR RESPONDENTS

OPINIONS BELOW

The brief of Petitioners correctly states that the opinion of the District Court (R. 34-36) has not been officially reported, and that the opinion of the Court of Appeals (R. 50-54) is reported in 203 F. 2d 690.

JURISDICTION

The brief of Petitioners correctly states that judgment of the Court of Appeals was entered on April 27, 1953 (R. 55); that petitions for rehearing were denied on July 27, 1953 (R. 55); that petition for writ of certiorari was filed in this Court on October 21, 1953, and granted on December 7, 1953.

QUESTION PRESENTED

Here Respondents part company with Petitioners. The question as presented by Petitioners is so loaded with argument, as to be of no value as a question.[1] The question to be decided by this Court is whether oral communications containing false and fraudulent statements inducing the investment are required to be transmitted across a state line, where the mails are used after the signing of an executory contract to complete the transaction (by delivery of the deed, care contract, care statements inducing additional investments, and guarantee title policy[2]), to make Section 12 (2) of the Securities Act of 1933 available to a defrauded investor, as a means of relief.

Also, alternatively, if Respondents are not entitled to the relief provided under Section 12 (2), then can jurisdiction be maintained under Section 17 (a) (R 2, 13)?

STATUTES INVOLVED

Section 12 (2) of the Securities Act of 1933, as amended, 15 U.S.C. Sec. 77 1 (2) reads as follows:

"Any person who—

* * * * *

sells a security (whether or not exempted by the provisions of section 3, other than

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[1] Note the use of the words, "local land dispute," "purchasers of citrus land in the Rio Grande Valley of Texas", "seek to invoke", "purely intrastate transaction", "where sale is completed without use of the mails or interstate commerce" and "executed documents evidencing a completed transaction", which in each case ask the Court to presume matters hotly contested in the pleadings herein, as will be apparent from further reading herein.

[2] The pleadings do not make special issue of the delivery of the guarantee title policy through the mails, though it will be shown at the trial that the promise of such delivery through the mails was a vital inducement to the investor to part with his money without first consulting an attorney.

paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security."

Section 17 (a) (2) of the Securities Act of 1933, as amended, 15 U.S.C. Sec. 77q (a) (2) reads as follows:

(a) It shall be unlawful for any person in the sale of any securities by the use of any means or instrumets of transportation or communication in interstate commerce or by use of the mails, directly or indirectly—

(1) * * * *

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in

order to make the statements made, in the light of the circumstances under which they were made, not misleading, or - - - -

Sections 2(3), 5(a) and (b), 13 and 15 are set out in the Appendix to this brief.

STATEMENT OF THE CASE

This action was originated in the United States District Court for the Southern District of Texas, Brownsville Division, by eight resident plaintiffs against these three Petitioners and twelve other corporate and individual defendants, all residents of Texas, (R. 1). The eight plaintiffs and a later intervenor (R. 26, 28) sought relief under the Securities Act of 1933 for cancellation and rescission or damages resulting from their purchase from defendant, Pummill Development Company and Pummill Management Company, of certain investment contracts in the form of contracts for sale of land, coupled with contracts for planting of said land to citrus trees and for care and management of such land and trees until maturity, and thereafter, with the purchasers to return to the place of their residence and do nothing further than meet the care bills as they came in through the mails, and ultimately reap the dividends or benefits of the investment. (R. 1, 3-10, 16, 29-33).

Respondents, on various dates from November 23, 1949 through March 3, 1950, purchased the alleged investment contracts, which consisted of a deed to land in Hidalgo County, Texas, coupled with a care or management contract providing for the setting of the land to citrus trees and the care and management of such citrus development. The deed was from

Pummill Development Company, and the care contract with Pummill Management Company, which companies had identical stockholders and officers. (R. 1-10, 26-28). Seven of such Respondents received deeds to twenty acres of land each, (R. 3, 5-6-7-8-9-10), one to forty acres, (R. 27), and another to eighty acres, (R. 4). Four of Respondents are wheat farmers from Northwest Texas, one a cotton farmer from Greenville, Texas, one an engineer from Wisconsin, who moved to Texas after the purchase, one is a merchant from North Texas, and two are merchants from Central Texas. None of Respondents lived in, nor were familiar with the citrus producing area of Texas at the time of the purchases, and all looked upon the transaction as an investment, as it was represented to them to be. None bought with the intention of personal management, but each relied upon the management of Pummill Management Company under the management contract. (R. 2, 3-10, 26-28).

Petitioners acquired title to an 800-acre tract of dry land worth approximately $50.00 per acre, and conveyed such land (less minerals) to the insolvent Pummill Development Company for nothing down, and a mortgage $100,000.00 in excess of the actual value of the land.[3] (R. 2, 13). This transaction gave petitioners control of the entire operation, forced Pummill Development Company to sell the land at prices still higher above the actual value of the land, and removed Petitioners one corporation (and a few brokers, etc.), further from the defrauded investors.

[3] It will be shown on trial that Petitioners have foreclosed on all, or substantially all, of the assets of Pummill Development Company, and Pummill Management Company, thus confirming Respondent's contentions of insolvency of the selling group and control by Petitioners.

(R. 2, 13). Thus the 800-acre tract could be uniformly developed as a unit, and offered for sale in small acreages with care and management contracts to investors, in the same manner as any other new issue of securities, at prices absorbing a pro-rata part of the original cost of the land plus the amount that was necessarily added as profit for Pummill Development Company.[4] (R. 2, 13, 14).

Respondents contend that their investments were induced by false and fraudulent oral representations and concealments made by brokers, officers, agents and employees of Pummill Development Company, and that continuing investments in care were induced by written fraudulent statements transmitted to Respondents through the United States Mails by both Pummill Management Company and Pummill Development Company, their officers and employees. (R. 2, 3-10, 10-15).

The division of labor involved in the selling operation was: (1) the broker's job was to find the prospect and bring him to the Clubhouse office of Pummill Development Company in the Rio Grande Valley of Texas; (2) there the officers and employees of said company would take over and complete the selling procedure with continued cooperation of the broker. (R. 2, 14, 15). An executory contract was signed and the investor's money taken in face to face negotiations at such time and place. Simultaneously it was agreed that the U. S. mails would be used to complete the transaction. Petitioners in

[4] It will be shown on trial that some of the items of additional cost include a 25% commission to the broker responsible for bringing the prospect to the Clubhouse of the selling group in the Rio Grande Valley, the cost of maintenance and operation of said Clubhouse, its staff of cooks, housekeepers, drivers for tours, and such profit as was calculated for the selling group.

their brief like to use language that the "transactions were thus completely entered into and all agreements made and concluded by face to face personal discussions in Hidalgo County, Texas, without use of the mails or any means of interstate commerce." (Petitioners' Brief, p. 5). Petitioners state as a fact that the transaction is closed when the selling company gets the investors' money or property, while Respondents state as a fact that the deal is not closed until the investor receives what he bought and paid for. These items are delivered to the purchaser through the mails, and include (1) the deed, (2) care or management contract, (3) guarantee title policy on the land,[5] and (4) numerous statements of care expenses, to induce further and continuing investment, which later statements included false and fraudulent matter. (R. 2, 3-10, 14).

The above use of the mails is not the sole basis of jurisdiction claimed by Respondents, as stated in Petitioners' brief (p. 5). Respondents also claim jurisdiction under Section 17 (a) of the Securities Act. (R. 2, 13).

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[5] It will be shown at the trial that the selling methods of Pummill Development Company included keeping the investor at the Clubhouse, some seven miles from the closest town, and isolating him from local prices, local conditions, and local people, for a period of three days, with the 3rd day being set aside for closing. The slightest contact with local real estate dealers, local attorneys, or local people during this closing period might appraise the investor of the true facts, and destroy chances of a sale. The selling company is in a position to tell the prospect that a guarantee title policy, his deed, and care contract will be transmitted to him through the mails, and after taking the investor's money or property, place him in an automobile with the broker who brought him to the Rio Grande Valley where he will be taken straight home hundreds of miles from his investment. This gives the selling company time to clear all checks without danger of the investor learning the true facts. The importance of this use of the mails in perpetration of the fraud cannot be ignored.

THE RULINGS BELOW

The District Court (Allred, J.) dismissed the complaint (R. 46-7) and in his memorandum gave as his reasons: (1) "the transactions alleged do not constitute a 'security' within the meaning of the act"; (R. 38); (2) that the use of the mails involved did not come within the prohibition of Section 12 (2) of the Securities Act, following the reasoning of Kemper v. Lohnes, 7th Cir., 173 F. (2d) 44, and rejecting the doctrine of Schiller v. H. Vaughn Clarke & Co., 2nd Cir., 134 F. (2d) 875, (R. 41-45) and adding this statement:

> "In view of this disposition it is unnecessary to discuss the remaining questions raised by defendants." (R. 45).

Having thus disposed of the case, the Court entered an order of dismissal without discussion of the question of jurisdiction under Section 17(a), which section would have application only if sale of a "security" were involved.

The Court of Appeals, 5th Circuit, reversed on both points, holding the complaint adequately alleged sale of a security, and use of the mails sufficient to bring the case under the provisions of Section 12 (2) of the Securities Act. (R. 50-55). Such holding automatically revived the importance of Section 17 (a) as a jurisdictional basis.

While Certiorari here was sought on the question of construction of Section 12(2), nothing contained in the Courts' Order Allowing Certiorari excluded consideration of the undecided question of the construction of Section 17 (a) of the Securities Act. (R. 56).

SUMMARY OF ARGUMENT

1. Section 12 (2) of the Securities Act gives a civil remedy where the mails are used for transmission of the deeds, care contracts, title policies, and care statements inducing additional investments. This Section does not require that the false statement or fraudulent matter be transmitted through interstate channels as an inducing factor, but only that the mails be used in connection with the transaction. Respondents contest the major premise of Petitioners' brief that the use of the mails in this case was *after* the sale was concluded, and contend that the sale is not "concluded" until the investor gets what he bargained for, which items were delivered through the mails in this case. Nevertheless, *after* the fraudulent sale, use of the mails as here involved is within the prohibitions of the Securities Act, as interpreted by the Court of Appeals, 2d Cir., in Schiller v. H. Vaughn Clarke & Co., 134 (2d) 875, and by the 5th Cir. in Blackwell v. Bentsen, 203 F. (2d) 690. Petitioners' construction of Section 12 (2) would throw this section out of alignment with the interpretation given other sections of the Act, as well as the general purpose of the Act.

2. Respondents are not afforded the relief under Texas Blue Sky laws, nor the common law of fraud, that is afforded by the Securities Act, and even if so, would not thereby be denied specific relief provided by Congress. Where there is an option as to relief available, it is not only the privilege, but the duty of Counsel for the injured party to select the relief which affords the injured party the greater protection. In this case it is the Securities Act in the Federal Courts.

3. Federal Jurisdiction was provided by Congress to give relief to injured parties in cases of this type, and the exercise of such jurisdiction by the Federal Courts is not an "extending" of such jurisdiction. To deny federal jurisdiction here would be a retrenchment from the intent of Congress to stop fraud in sales of securities, and the interpretations of the Courts of such intent.

4. The Congressional purpose in pasing the Securities Act was, among other things, to prevent the use of the mails as an auxiliary to any scheme for fraudulent sale of securities. Such purpose would be served by affirming the judgment of the Court of Appeals.

5. Respondents contend further that they are entitled to relief in the Federal Courts under the provisions of Section 17 (a) of the Securities Act which renders the use of the mails here involved unlawful. The District Court having held no security was sold, did not pass on Section 17 (a); the Court of Appeals in reversing the District Court, held that sale of a security was involved, and that there was sufficient use of the mails to bring the transaction within Section 12 (2), and did not rule as to Section 17 (a). Respondents contend further that if this Court finds no jurisdiction under Section 12 (2), it must rule as to Section 17 (a), in order that justice may be done in this matter, and uncertainty removed from the law.

ARGUMENT

I. The Statutory Language Does Apply to the Facts Pleaded Here

The District Court's memorandum contained a quotation from the brief of Pummill Development

Company, et al, in the District Court, wherein Respondents (Plaintiffs below) were accused of "having read some cases," and then attempting to plead themselves into Federal Court. (Petitioners' Brief, p. 6). Petitioners like to quote this statement, and Respondents like to plead guilty of "having read some cases". The decision of this Court in S.E.C. vs. W. J. Howey Co., 328 US 293, is on all fours with the facts involved in the instant case, with the exception that the Howey Co. was apparently engaged in a good-faith, legitimate operation. The District Court's effort to distinguish it implies a doctrine that if the swindle involves a small amount (one row of trees), it violates the Securities Act, but if a large amount, (20 acres), the Securities Act is impotent. (R. 40).

The petitioners in this case, like the Howey Co., had failed to register their operation with the Securities and Exchange Commission. The plaintiffs-respondents, because of the false reports and statements forwarded to them at their homes in distant parts of Texas by the sellers, remained in ignorance concerning the fraudulent nature of their investment for more than the 12 months limitation period after their purchases to bring action for failure to register, and were forced to bring their suit under Sections 12 (2) and 17 (a) of the Securities Act instead of Section 12 (1), which provides for a private right of action for failure to register the Securities.

Because of the one-year limitation statute applying to Section 12 (1), Respondents read further as to Sections 12 (2) and 17 (a), and found that the Second Circuit Court in the case of Schillner vs. H. Vaughan Clarke, 134 Federal (2d) 875, had held that

a delivery of securities through the mails after the securities had been paid for, was a sufficient use of the mails to allow recovery under Section 12(2).[6] Since it was part of the arrangement that the plaintiffs-respondents, in addition to receiving Warranty Deeds, guarantee title policies and care contracts from the defendants through the mails, were to receive and did receive through the mails, statements which induced additional investments in the property, which statements included false and misleading reports of care and management, it was felt that jurisdiction did lie in the Federal Courts under the Securities Act, and that this was the most effective and complete relief available to the plaintiffs-respondents.

1. Section 12(2) does not require that the false statements concerning the security sold be transmitted through the mails.

Petitioners assume in their argument that the false and fraudulent statements inducing the purchase must be transmitted by some means of interstate commerce before there can be any liability under Section 12(2). This requirement is simply not contained in the wording of the statute, and may only be placed there by implication. As we shall show below, the complaint does allege the transmission of false and fraudulent information through the mails by way of the fraudulent and false statements for care and reports on care that had been given the property. It is easily demonstrated that this section does not require that the false state-

[6] The District Court in dismissing the complaint recognized that Plaintiffs had read this case right, stating "There is authority for both views". (R. 42).

ments be transmitted through or by means of interstate commerce.

Section 12(2) of the Securities Act as finally passed by Congress, while not a model of draftmanship, clearly applies to the case at bar. In order for it to be applied as Petitioners urge requires more to be read into it than is required by the interpretation and application made by the Court below. Nor is the application sought by Petitioners in keeping with the intention of Congress as expressed in the entire Security Act.

Boiling the problem down to its simplest point, the question is, do the false and fraudulent oral statements inducing the investor to make his purchase, have to be transmitted by interstate telephone or radio, before the relief given in Section 12(2) can be used by investors who have been defrauded? We think not.

The Section as construed by the Court below reads as if the word "and" were implied between the second and third clauses, as follows:

> Any person who—
>
> (2) sells a security — by the use of any means or instrument of transportation or communication in interstate commerce or of the mails *(and)* by means of — oral communication which includes an untrue statement of a material fact — shall be liable, etc.

This interpretation is the most natural and logical application of the Act, and prohibits the use of the mails at any stage of the transaction.

In order to construe the section as urged by Petitioners, it is necessary to imply much more than

this into the language used by the Congress. The language used does not state that the false oral communication must be transmitted in interstate commerce, so to arrive at the interpretation urged by them it is necessary to imply the following:

> Any person who—
>
> (2) sells a security — by the use of any means or instrument of transportation or communication in interstate commerce or of the mails, by means of — oral communication *(transmitted by said means or instruments of transportation or communication in interstate commerce or of the mails)*, which includes an untrue statement of a material fact — shall be liable, etc.

The construction urged by Petitioners is possible only if Section 12(2) is isolated from the other anti-fraud provisions of the Act and is not read as a part of the overall plan. It would eliminate any actions based on the ordinary "oral communication", and by the simple process of avoiding telephone conversations or radio messages across State lines, the confidence men and swindlers can and will avoid any liability under the securities act, although they are and will be using the U. S. Mails to transmit all of the documents, contracts, deeds, etc., evidencing their transaction. Such a construction would imply a Congressional intent to pave the road for the confidence man and swindler by setting up a legal way in which their activities could be carried on with the full use of the Post Office Department and all its facilities.

Petitioners assume in their argument that the mails have to be used *before* the investor has been induced to sign on the dotted line, or part with his

money, in order for Section 12(2) to apply. In other words, if the seller can get the investor to part with his money or sign a purchase money note without using the mails, then any subsequent use of the mails in consummating the deal is not a part of the definition of "sells". They then discuss the fact that Section 5 of the act provides both for a "sale" and for "delivery after sale", and that since Section 12(2) does not provide for "delivery after sale", that it cannot be read into the definition.

We believe this is wrong. Section 12(1) provides a remedy for any violation of Section 5. Section 5 (a) (1) provides a penalty for the sale of a security, and Section 5 (a) (2) provides a penalty for the delivery of a security after sale. If the word "sell" in Section 12 does not include delivery after sale, then Section 12(1) would only apply to violations of Section 5 (a) (1) and would not cover Section 5 (a) (2). We do not believe that this was intended by Congress, and certainly under the definition of "sale" in Section 2(3), "delivery after sale" would be included and govern the definition to be used in Section 12(1) and (2).

The Second Circuit in Schillner vs. H. Vaughan Clarke, 134 F. 2d 875 fully discussed the statute involved, and stated:

> "In the case at bar the contract of sale was concluded orally and the stock was paid for by the buyers without any use of the mails, but the mails were used for delivery of the stock certificates to the buyers. In our opinion such a transaction falls within both the letter and purpose of the statute. Section 2(3) of the Act, 15 U.S. C.A. Sec. 77b (3) provides that "unless the con-

> text otherwise requires" the term "sale" or "sell" shall include every contract of sale or disposition of * * * * a security or interest in a security for value". Delivery of the stock certificate pursuant to a contract of sale would seem to be a "disposition of * * * * a security" within this defination; consequently the seller who mails the certificate to the buyer "sells a security * * * by the use * * * of the mails".

The complaint in this case in addition to the allegations concerning the misrepresentations and fraud inducing the original purchase of the land, trees and care contracts, also alleges the mailing of statements for care expended on the "investment" together with reports of what had been done by the Defendants. These statements contained false reports as to what had been done, and that good irrigation water had been used on said trees, when such water was neither used by the Defendants or available to them for use. (R. 13). These additional mailings were the inducing cause of a further or continuing investment by Respondents in the "security" or "investment contract", and are in the nature of "prospectuses". Certainly if the true facts had been contained in such statements and reports, the Respondents would not have invested any more money in the property.

Petitioners briefly mention the Schillner case and argue that the Security Act was aimed only at Securities Sales in interstate commerce, and that the construction of the statute by the Court in that case was as though it were adopted by a local government rather than a federal government. We need not emphasize to this Court that the purpose of the

Securities Act was to *stop fraud* in the sale of securities, and that the required use of interstate commerce facilities was merely a necessary jurisdictional prop, and not a barrier to the Courts in *stopping such fraud.* The Schillner opinion is in keeping with the purpose and intent of the act, is justified by the wording of the statute, and will deter, if not prevent, the perpetration of fraud in future security transactions.

At the time the parties (Pummill and Respondents) affixed their signatures to the sales contract in the "face to face" transaction, so cherished by Petitioners as excusing them from compliance with the Securities Act, there was much yet to be done to deliver to the purchaser what the purchaser had bargained to receive. Under no stretch of the facts could physical delivery of the deed even give purchaser title to the land described therein, when the mortgage of Petitioners, (which under Texas law is superior title), was still against the property. The Purchaser was making a continuing investment in land, trees, and care and management. By what magic is the deal closed until he has his trees planted, and a caretaker in charge? Even accepting Petitioners' elusive logic that the deal is closed when the selling company gets the purchaser's money or property, seller's right to retain the money paid for planting land to trees does not mature until the trees have been planted. In the meantime, while this executory state of affairs exists between buyer and seller, the uses of the mail here involved take place, with the exception of the use to transmit statements for care of the trees, which statements precede and induce additional investments. The investor (Re-

spondents) bargained for a producing citrus grove as a part of a uniformly developed 800-acre tract, to be developed over a five year period. Can the deal in fact be considered closed until a five year period of the care contract is up, and the investor has received in full the subject matter of his original bargain paid for in part at the time, and in part over the five year period, based upon statements for care and expenses transmitted through the mails during such continuing period of investment?

(2.) Petitioners interpretation of Sec. 12(2) would throw it out of alignment with other sections of the Securities Act.

If it is held that the misrepresentations or fraudulent statements must be sent through the mails, then the Defendants herein might be liable for a criminal offense under the Act and yet not be liable civilly. Section 17 (a) (2) makes unlawful the types of misrepresentation and fraud set out in the complaint in this case, and the only requirement for use of the mails is that it be used at some point in the transaction. Set out below are some of the examples of mailings that have been held sufficient.[7] It is evident that the use of the mails is required only to give the necessary jurisdictional basis for the Federal Courts to act.

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[7] Mailing of reports among the Defendants reporting the success of meetings held to obtain money from victims, and remitting the proceeds. U.S. v. Monjar, 47 F. Supp. 421, aff'd, 147 F. 2d 916 (C.A. 3, 1944), cert. denied, 325 U.S. 859 (1949).

Delivery by mail of stock certificate after sale by oral representations. S.E.C. v. Wimer, 75 F. Supp. 955.

Mailing of warranty deeds between defendants, and to the county clerk for recording and delivery to investor. Mansfield v. U.S., 155 F. 2d 952 (C.A. 5, 1946), cert. denied, 329 U.S. 792 (1946).

Mailings acknowledging part payment and transmitting deeds. U.S. v. Earnhardt, 153 F. 2d 472 (C.A. 7, 1946), cert. denied, 328 U.S. 858 (1946).

There is nothing in the wording of Sec. 12 (2) or elsewhere in the Act to indicate that Congress intended to limit jurisdiction as to this provision, or make it more narrow than the other anti-fraud provisions of the Act. It is also evident that the purpose of the entire statute is to afford broad pratection to investors, and the statute being remedial in nature, should be construed to achieve that purpose.

Referring again to the Howey case, this Court at Page 301, in rejecting the theory that an investment must be speculative before it constituted an investment contract under the Act, stated:

> "The statutory policy of affording broad protection to investors, is not to be thwarted by unrealistic and irrelevant formulae".

The Fifth Circuit followed this policy in the decision below, and there is certainly no less reason for protecting investors today than there was in 1946, when the Howey case was decided.

II. Investors Will Lose A Large Part of the Protection Afforded By The Statute Under Petitioners Interpretation

We take issue with Petitioners on their statement that there is no question of the protection of investors involved here. Assuming that it is held that no private action will lie under Sec. 17 (a) of the Act, then the investors are restricted to Sec. 12 of the Act. Further assuming that the registration provisions of Section 5 are complied with by the promoters, then they could make any use of the mails they desired so long as they didn't transmit any false statements in the mails, and didn't engage in any "sales" talk by long distance phone or radio across state lines.

This, in our opinion, would assure the swindlers and confidence men of success in their operation, because it is common knowledge that the greatest swindles of all are effected by the "glowing pictures painted by the silky tongue of the confidence man". In other words, by "oral communication in a face to face transaction".

Petitioners view would allow these men to send through the mails to investors invitations to visit the Clubhouse, and evidence of the visit after their return to their homes without fear of civil liability. We do not think this was the purpose for which the Securities Act was passed. We do not read into the Securities Act a Congressional intent to set the swindler and confidence man up in a Garden of Eden, with only one forbidden fruit: use of mails to transmit the false representation or information.

Petitioners further argue that the Plaintiffs have full and complete protection under the Texas Blue Sky Law. We respectfully submit that the Texas Act provides only for actions against the Seller, has no provision covering the persons controlling the Seller,[8] and requires a much stronger burden of

[8] As is alleged in the complaint, and as will be shown at the time of trial, Petitioners operate through insolvent selling corporations. In this case, they used Pummill Development Company, a $1,000.00 corporation, which corporation they put $100,000.00 in the hole when they conveyed the 800-acre tract in question to such company, with no down payment, reserving a mortgage for $100,000.00 in excess of the value of the land. A judgment against Pummill Development Company, under such circumstances, would be worthless. Petitioners, with their mortgage, could and would wipe Pummill Development Company and all its assets off the face of the earth right under the auctioneer's gavel, should a successful plaintiff seek execution under such a judgment against the selling company alone. Consequently, Petitioners, who stand behind and take the bulk of the money out of the selling operations, and control it from a position of simulated remoteness, must be made parties to the action. This so complicates the suit as to almost price justice out of the market to the defrauded investor (under Texas law). The Securities Act, (Section 15) has provided for reaching those who control the Sellers, thus giving them

proof on the part of the Purchaser.

Counsel for Petitioners also state that counsel for Plaintiffs-respondents have had other cases involving Petitioners in Federal Court based on diversity of citizenship and that in those cases relied on the Texas Common Law of Fraud.[9] This is admitted, but the reason the Securities Act was not mentioned was that the Plaintiffs in those cases made their arrangement for care with third parties and hence the test of an "investment contract" as established by this Court in the Howey case was not met.

Under Article 4004 of the Revised Civil Statutes of Texas, a defrauded purchaser is allowed to recover the difference between the value of the property sold as it actually existed, and as it would have been if it had been as represented. This is an inadequate remedy, because in the instant case the complaint alleges that the actual value was $100.00 per acre, and the Petitioners, to lessen their damage would argue that if it had been as represented, it

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some hope in financing their actions, as well as the outcome. From our point of view, instead of Respondents reading some cases, and pleading themselves into Federal Court, the Petitioners, in backing off from the Texas Blue Sky Laws and Common Law of Fraud, backed into the Securities Act of 1933.

[9] Petitioners' brief makes frequent reference to the fact that Counsel for Respondents have represented other plaintiffs against petitioners, wherein violation of the Securities Act was not alleged as the basis of Federal jurisdiction, implying that the purpose of such pleading is to invoke Federal jurisdiction. Thereby Petitioners invite, if not provoke, a statement of the whole facts by Counsel for Respondents. Of twenty-five cases wherein Counsel for Respondents have represented Plaintiffs against Petitioners, nine plaintiffs were residents of Texas at the time of both the sale and the filing of suit, and their cases filed in the State Courts; three were residents of other states at the time of sale, but were residents of Texas at the time of the suit, and their suits were filed in State Courts; one was a resident of another state at the time of the sale and filing of the suit, and his suit filed in the State Courts; and twelve were residents of other states, and their suits filed in Federal Court based on diversity of citizenship. The residence of these plaintiffs as of the time of the sale was: Iowa, 6; Indiana, 1; Ohio, 3; Minnesota, 1; California, 1; Tennessee, 1; Oklahoma, 2; Illinois, 1; and Texas, 9. This indicates no tendency to invoke Federal jurisdiction on trivialities, as well as illustrating the interstate nature of Petitioners' operations.

would only have been worth $200.00 per acre. The purchasers actually expended $400.00 per acre for the land, plus the cost of the trees and care. Under the Security Act of 1933, the purchasers are entitled to a return of all of their purchase money, which is certainly more relief than is provided by any action available in the State Courts, with the exception of course, of complete rescission.

Under Petitioners' interpretation of Section 12 (2), it would make no difference whether the Purchaser of a security lived in New York or California, as long as the promoters did not actually transmit the misrepresentations through interstate commerce prior to obtaining his signature on the purchase agreement, regardless of how many falsehoods were related orally in inducing the purchase in the "face to face" transaction. In that event, his only remedy would be under State Laws, and he would be denied any relief under the Securities Act, irrespective of the use of the mails in consummating the deal through delivery of the securities.

III. The Ruling Below Does Not Extend Federal Jurisdiction But Follows The Intention of Congress to Suppress Fraud in Security Transactions:

Petitioners complain about a recent ruling of the 9th Circuit Court in which a promissory note was held, under the definition of a "security" in Section 2(3) of the Act, to constitute a security. An examination of that case shows that it was a criminal prosecution under Section 17 (a) (1) of the act, and that it involved a plan or scheme to defraud under which the Defendant was extracting sums of money by fraudulent means from a large number of people,

and giving worthless promissory notes in exchange therefor. Fear is expressed by the Petitioners that if the decision below is allowed to stand combined with the finding that a note is a security, next door neighbors who fall out over a land deal would immediately drop their papers in the mail box and rush into the nearest Federal Court.[10]

Respondents' answer that, in the first place, the ordinary transaction involving promissory notes is handled on a personal basis, and is not dependent on the mails for its successful consummation. In the second place, if fraud is involved in the sale of an instrument which is a "security" under the definition of the act, and such instrument is transmitted through the mails or by some other means of interstate commerce, then Congress gave that individual a right in Federal Court, and the Courts will just have to put up with him.

Respondents are not unsympathetic with the overworked Judiciary, but reject the idea that it ever has been, or ever will be the attitude of our Courts to avoid doing justice merely because of the hazards of overwork which might result from the influx of others likewise seeking justice. Petitioners overlook the fact that a clear cut decision hitting a fraudulent operation a mortal blow, quite often eliminates future similar work by eliminating the evil.

Petitioners further imply that the Securities Act should be broadly construed where the S.E.C. and

[10] Actually, the Courts are quite competent to protect themselves against the possibility of neighbors taking local squabbles into Federal Court. Petitioners hold before the Court the picture of a Federal Judiciary entangled in a mass of neighborhood squabbles, but the cases they cite as tending in this direction seem, in each instance, to involve the culprit who was operating a fraudulent scheme of interstate proportions, though the false representations were made face to face.

the Attorney General are concerned, but that private litigants, lacking the discretion of Governmental Agencies and Officers, should be restricted. This argument is untenable, for the sole purpose of the Securities Act is to protect the investors, the persons who pay the salaries of the enforcers of said Act. If they are to be protected, a double standard of interpretation is not the solution.

IV. Congressional Purpose is Served by the Construction of The Statute Adopted by the Court Below

Quotations from one or more legislators adverse to any worthwhile legislation are always available. But the overall, prevailing legislative intent is best determined by a common-sense application of the language they approved as a body to the purpose they intended to accomplish. The Federal Judiciary has said much about the purpose and intent of the Securities Act. Every expression of the judiciary concerning the Act has been that *the purpose was to stop fraud in the sale of securities.* The previously quoted statement of this Court in the Howey case was in keeping with the statement in S.E.C. vs. Joiner Leasing Corp., 320 U.S. 344, at 350-351, concerning statutory construction:

> "Some rules of statutory construction come down to us from sources that were hostile toward the legislative process itself and thought it generally wise to restrict the operation of an act to its narrowest permissible compass. However well these rules may serve at times to aid in deciphering legislative intent, they long have been subordinated to the doctrine that courts will construe the details of an act in conformity

with its dominating general purpose, will read text in the light of context and will interpret the text so far as the meaning of the words fairly permits so as to carry out in particular cases the generally expressed legislative policy".

There is no clearer case for the application of the above doctrine than in the interpretation of Section 12(2). That the holding of the Court below is in keeping with this doctrine, and the expressed legislative policy of Congress, cannot be denied.

V. Jurisdiction for Private Relief Under Section 17 (a)

The Petition for Certiorari was granted on Section 12(2) of the Securities Act. However, Plaintiffs in the original complaint based jurisdiction also on violation of Section 17 (a). The trial Court, having held that the Complaint did not allege the sale of a security as defined by the Act, and that no use of the mails under Section 12 (2) had been alleged, did not rule on the relief sought under Section 17(a). The Circuit Court, having reversed the Trial Court on both of the findings so made, and remanded for trial, did not rule on Section 17(a). Plaintiffs are now in the position that if this Court should reverse the Circuit Court on Section 12(2), without passing on the relief available under Section 17 (a), the Complaint would be dismissed although under the ruling of the Circuit Court the sale of a Security was involved. Therefore, in order that Justice may be done, Plaintiffs-Respondents here, respectfully submit that it is necessary that this Court also rule on the alternative relief available to them under Section 17(a).

It is basic tort law that a person who has been injured by the violation of a statute intended for the protection of a class of which he is a member, may maintain a civil action for private relief. This is true unless the statute itself prohibits such an action, or unless there is other provision made for redress which is not inconsistent with the rule. This rule has been followed in allowing private actions for the violation of provisions of the Securities Act of 1934.

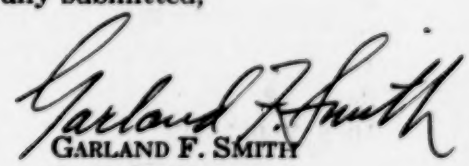
In Osborne v. Mallory, 86 F. Supp. 869 (S.D.N.Y. 1949) the court in discussing Section 17 (a) expressly stated that the investor had an implied right of action for the violation of Section 17 (a). It is therefore respectfully submitted that the instant Plaintiffs have a right to maintain this suit for their damages under Section 17(a) even if it is held that they do not have such right under Section 12(2).

CONCLUSION

The legislative intent, the language of the statute, and the holdings of the Courts relied upon by Respondents are all consistent with a cause of action in Respondents as pled here. The transaction was not complete at the time of the use of the mails, and if so, the use of the mails here involved is so integral a part of the transaction as to bring the matter within the Securities Act. The remedy afforded by local law is not adequate, and if it were, such fact would not deprive Respondents of the benefit of the Securities Act. The decision below does not extend federal jurisdiction, but pursues the common sense meaning of the Securities Act. Careful interpretation and enforcement of the Securities Act will greatly reduce

the dockets of federal courts by eliminating the evil of fraudulent sales of securities, whereas interpretation permitting use of the mails at all phases of the transaction except in transmitting the false matter, will through uncertainty give rise to more litigation, and fall short of accomplishing the legislative purpose to prevent fraud in sales of securities. The judgment of the Court of Appeals should be affirmed with directions that the case be remanded to the District Court for trial in accordance with such opinion of the Court of Appeals, and such additional direction as this Court shall deem proper.

Respectfully submitted,



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APPENDIX

Section 2 (3) of the Securities Act of 1933 (15 U.S.C. Sec. 77b (2)) reads as follows:

> Sec. 2 (') The term "sale", "sell", "offer to sell", or "offer for sale" shall include every contract of sale or disposition of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value; except that such terms shall not include preliminary negotiations or agreements between an issuer and any underwriter. Any security given or delivered with, or as a bonus on account of, any purchase of securities or any other thing, shall be conclusively presumed to constitute a part of the subject of such purchase and to have been sold for value. The issue or transfer of a right or privilege, when originally issued or transferred with a security, giving the holder of such security the right to convert such security into another security of the same issuer or of another person, or giving a right to subscribe to another security of the same issuer or of another person, which right cannot be exercised until some future date, shall not be deemed to be a sale of such other security; but the issue or transfer of such other security upon the exercise of such right of conversion or subscription shall be deemed a sale of such other security.

Section 5 (a) and (b) of the Securities Act of 1933 (15 U.S.C. Sec. 77e) reads as follows:

> "Sec. 5 (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation any such security for the purpose of sale or for delivery after sale.

(b) It shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security registered under this title, unless such prospectus meets the requirements of section 10; or

(2) to carry or cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of section 10."

"Sec. 13 of the Securities Act of 1933 (15 U.S.C. Sec. 77m) reads as follows:

Sec. 77m. Limitation of actions

No action shall be maintained to enforce any liability created under section 77k or section 77 1 (2) of this title unless brought within one year after the discovery of the untrue

statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence, or, if the action is to enforce a liability created under section 77 1 (1) of this title, unless brought within one year after the violation upon which it is based. In no event shall any such action be brought to enforce a liability created under section 77k or section 77 1 (1) of this title more than three years after the security was bona fide offered to the public, or under section 77 1 (2) of this title more than three years after the sale.

Sec. 15 of the Securities Act of 1933 (15 U.S.C. Sec. 77o) reads as follows:

Sec. 77o. Liability of controlling persons

Every person who, by or through stock ownership, agency, or otherwise, or who, pursuant to or in connection with an agreement or understanding with one or more persons by or through stock ownership, agency or otherwise, controls any person liable under sections 77k or 77 1 of this title, shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person had no knowledge of or reasonable ground to believe in the existence of the facts by reason of which the liability of the controlled person is alleged to exist.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., ET AL., *Petitioners*,

v.

EMERY C. BLACKWELL, ET AL., *Respondents*.

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March, 1954.

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LLOYD M. BENTSEN, SR., ET AL., *Petitioners,*

v.

EMERY C. BLACKWELL, ET AL., *Respondents.*

REPLY BRIEF FOR PETITIONERS

The main issue is joined clearly by the briefs already filed in this action. Petitioners contend that in Section 12(2) of the Securities Act, Congress did not intend to govern face to face local securities transactions wherever the mails were used incidentally, as here, to deliver evidence of a previously concluded sale. Respondents and amicus curiae on the contrary say the Act was intended to apply in such cases. Petitioners contend that the Act contemplated an approximate accommodation between local and national matters allowing local transactions to remain within the competence of the states to be handled under state authority, and extending federal power and jurisdiction only to cases which seemed of national consequence. We believe

that the language of the statute and its history establish that the Congress was proceeding with an intention to limit federal jurisdiction so that it was not exercised "beyond the need of public protection". H. Rep. No. 85, 73d Cong. 1st Sess. p. 7. We do not suggest that the line was drawn as sharply as it might have been drawn today, for constitutional problems had their effect upon the scope of the Act (See Pet. Br. pp. 23, 24). But the objective of the statute is, we submit, clearly one based on the federal nature of our governmental system.

The language of the section requires the petitioner's suggested construction and the purpose of the statute will be advanced by such a construction.

I. PETITIONERS' CONSTRUCTION IS REQUIRED.

a. *Section 17 (a) of the Securities Act of 1933 and Section 10(b) of the Securities Exchange Act of 1934 are not analogous.* The amicus brief argues that Section 17(a) of the Securities Act of 1933 and Section 10(b) of the Securities Exchange Act have language which does not require as close a connection between the subject matter of the section and the use of the mails as does Section 12(2) here involved. From this premise, they argue the dubious conclusion that Section 12(2) should be construed as though its concededly different language is identical with those other sections. Of course, this argument ignores the fact that the sections are differently phrased. It also ignores the fact as pointed out in our main brief (pp. 14, 15) that the sections have different purposes and that the policy considerations are different. It takes no account of the fact that this Court has never construed the other provisions mentioned so broadly as is contended for in the present case. Indeed, even the lower court opinions on the other sections mentioned do not support respondents' position. No assistance in construing Section 12(2) can be obtained from a consideration of Section 17(a) of the 1933 Act or Section 10(b) of the Securities Exchange Act of 1934.

(1) Amicus curiae is aware of the substantial difference in language between the Sections now urged to be parallel. It has even on other occasions urged on the courts a position contrary to that urged here. Thus it has persuaded the Ninth Circuit Court of Appeals to adopt the position that the sections now urged to be parallel should be construed without regard to Section 12(2). In response to the Commission's urging as amicus curiae, that Circuit, in *Fratt* v. *Robinson*, 203 F. 2d 627, 634 (CA 9 1953), comparing Section 12(2) and Rule X-10B-5 under Section 10(b) of the Securities Exchange Act of 1934, said:

> "The applicable statutes are different in the two cases, as will be seen readily upon comparing them. While it may be that the fraudulent acts must appear in the use made of the instrumentality under § 12(2) of the Securities Act of 1933, under the Securities Exchange Act of 1934 the use need only be 'in connection with' the fraud."[1]

(2) The amicus brief here abounds with statements that petitioners do not deny that this transaction would be covered by Section 17(a) of the Securities Act (e.g., pp. 10, 14). We do deny it. We make no such concession. We had not felt it necessary to argue the point because the language of Section 17 is different, the form of legal action contemplated is different and the policy considerations are different (Pet. Br. pp. 14, 15). But certainly there is no substance to the argument that Section 17(a), or even the more broadly phrased Rule X-10B-5, would apply in the present situation. We have pointed out that this Court has ruled that even the inclusive mail fraud statute would stop short

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[1] Thus the SEC's amicus brief in the Ninth Circuit, in *Fratt*, stated, e.g., at pp. 68, 69: "But the question as to the proper interpretation of Section 12(2) of the 1933 Act is not before this Court.

"The different language of Rule X-10B-5 does not give rise to such a controversy . . ."

"Section 17(a) of the 1933 Act, upon which the Rule [X-10B-5] is patterned, contains similar language."

of a case where as here "the investor's money [was] taken in face to face negotiations."[2] See *Kann* v. *United States*, 323 U.S. 88 (Cited in Pet. Br. p. 15).

The Commission cites a number of District and Circuit Court cases. Certainly no lower court cases should have any weight in this Court. Further, the lower court cases cited by the Commission and the respondents do not support the position claimed by them. There is not a single Court of Appeals case in which it has been held or even stated that delivery of securities after sale is a violation of Section 17.[3] Indeed, it seems that so far as the lower courts are concerned, the respondents are in as good a position under Section 12(2) itself as under the other provisions claimed to be analogous. In any event argument

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[2] The quotation is from p. 6 of Respondents brief.

[3] The cases cited in footnote 20 on page 24 of amicus brief and note 7 of respondents' brief are primarily mail fraud cases. The three Court of Appeals cases cited, for example, are cases of appeals from convictions under the mail fraud statute coupled with Securities Act or conspiracy counts. The cases contain no discussion of the language of Section 17.

Thus, *United States* v. *Earnhardt*, 153 F. 2d 472 (CA 7 1946) was a case of conviction on eleven counts of mail fraud, Securities Act and conspiracy. The opinion discusses exclusively the mail fraud statute and there is not a single word of discussion of Section 17.

Bogy v. *United States*, 96 F. 2d 734 (CA 6 1938) was a case involving an appeal from a conviction under five counts of violation of the mail fraud statute and a sixth count alleging conspiracy to violate the mail fraud statute and the Securities Act. There was no substantive Securities Act count. The case contains some slight discussion of Section 17 and although the facts are meager they indicate that the mails were used to obtain surrender of securities owned by a customer. Certainly the case did not involve a delivery after sale.

Mansfield v. *United States*, 155 F. 2d 952 (1946), also a mail fraud case, is from the Fifth Circuit which decided the instant case below. Although it may therefore be assumed that court would decide as the Commission has indicated, the opinion cited contained no discussion of the language of Section 17(a) or its requirements concerning the relationship of the use of the mails to the scheme to defraud or to the sale of securities.

by analogy is treacherous unless the parallel and the result are both clear. Here neither is. The question under 12(2) is not illuminated by consideration of the differently phrased sections mentioned.

b. *The legislative history has been misconstrued by amicus.* Amicus seeks to construe the legislative history as favorable to its view by asserting that the Senate due to "preoccupation" made an inadvertent "omission" of jurisdictional language in the Senate bill (Br. pp. 29, 30). The purpose is apparently to suggest that the Congress regarded the jurisdictional allegations of Section 12(2) as non-essential and they should therefore be construed as though they had not been inserted in the statute. The argument misconstrues the legislative history. The Senate bill deliberately and not by omission contained no jurisdictional language because that bill provided for civil liabilities only in the case of securities registered with the SEC under the Act. Jurisdiction in such cases, as in Section 11 of the Act as passed, was based upon the filing of the registration statement. Section 9 of the Senate Bill quoted *in part* in the amicus brief (Footnote 29 of page 29) gave a right of recovery to every person acquiring any security by reason of misrepresentations made in the distribution of "such securities", i.e., securities covered by a registration statement filed with the SEC. This is made clear when the previous two sentences of the Senate bill are read with the part quoted by the Commission.[4]

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[4] Section 9 of the Senate bill began as follows:

Sec. 9. Every person acquiring any securities specified in such statement and offered to the public shall be presumed to rely upon the representations set forth in the said statement. In case any such registration statement shall be false or deceptive in any material respect, any person acquiring any securities to which such statement relates, either from the original issuer or from any other person shall have the right to rescind the transaction and to obtain the return, either at law or in equity, of any and all consideration given or paid for any such securities

When the House Committee considered the matter, it determined that in addition to a section dealing with securities registered under the Act, it needed another section covering securities not so registered. It also considered that cases in which the misrepresentations concerning registered securities were not contained in the registration statement belonged more properly in the latter section. The House Committee therefore separated these problems in two sections, the present Section 11 dealing with misrepresentations in a registration statement, and Section 12(2) dealing with representations which might not be contained in the registration statement. In the case of false statements in the registration statement no jurisdictional language was used (§ 11), but in the other class of representations the Committee adopted the very careful jurisdictional basis which is now in Section 12(2).

The statute explains itself more readily if we assume Congress knew exactly what it was doing in providing a jurisdictional base for Section 12(2), rather than the contrary view, which is, as we have seen (Pet. Br. pp. 18) basic to the position of the respondents and amicus curiae.

c. *Means of transportation are appropriate means of carrying communications as well as securities.* Amicus mentions the fact that Section 12(2) talks about a *means of transportation* or communication in interstate commerce. Presumably, the point suggested, though not stated, is that

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upon the surrender thereof, either from any vendor knowing of such falsity or from the persons signing such statement, jointly or severally.

It is then followed by the sentence quoted by amicus as follows:

Every person acquiring any security by reason of any false or deceptive representation made in the course of or in connection with a sale or an offer for sale or distribution of such securities shall have the right to recover any and all damages suffered by reason of such acquisition of such securities from the person or persons signing, issuing, using, or causing, directly or indirectly, such false or deceptive representation, jointly or severally * * *.

securities can be delivered through means of transportation but that communications such as prospectuses cannot. This is of course not the case. The many methods of transportation, e.g., by messenger, by rail or air express service, etc., are equally adapted to the transportation of securities and communications such as prospectuses. If any doubt could exist on this point, Section 17(b) of the Act sets it at rest. For that section contains a prohibition of use of the means of transportation in interstate commerce although it deals exclusively with communications and not at all with securities.[5]

d. *Section 12(1) is not analogous.* The respondent and the amicus urge that the distinction between "delivery after sale" and "sale" contained in the statute (Pet. Br. pp. 11, 12) is inapplicable to Section 12. They argue that otherwise Section 12(1) would not give a remedy for sale illegal under Section 5(a)(2) solely because the securities were delivered after sale by use of the mails. We do not know whether this construction would be unreasonable or not. The argument that Section 12(1) must be coextensive with Section 5 runs into seemingly insurmountable difficulty when it is recalled that Section 5(a)(1) prohibits not only sales but also an "offer to *buy*". 15 USC § 77e(a)(1) But if the context so "requires" the word "sale" in Section 12(1) can be construed differently from the definition contained in Section 2(3) of the Act. However, if the context of Section 12(1) requires that violence be done to a definition, it does not follow that the same violence should be done in Section 12(2), where the context does not so

[5] Section 17(b) prohibits undisclosed paid publicity for securities and makes it unlawful "by the use of any means or instruments *of transportation* or communication in interstate commerce or by the use of the mails, *to publish, give publicity to, or circulate any notice, circular, advertisement, newspaper, article, letter, investment service, or communication which*, though not purporting to offer a security for sale describes such security for a" concealed consideration. 15 USC § 77q(b) (Emphasis supplied)

require. For the definitions contained in Section 2(3) are intended to apply in all cases, as the statute provides, "unless the context otherwise requires". Section 2, 15 USC § 77b.

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Amicus states (Br. p. 32) "In articles published shortly after passage of the Act, eminent authorities read Section 12(2) as did the court below," and cites articles by Douglas and Bates, by Frankfurter, and by Dean. The authorities are indeed eminent, but their articles are very far from supporting the bold statement made by amicus. Thus, one article contains no statement concerning the relation of Section 12 to the use of the mails at all.[6] Another merely contains a statement that "as a practical matter" "it will be safer" to construe the Act as applicable[7] and the third contains a most casual reference in a footnote.[8]

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[6] Justice Frankfurter's article, *The Federal Securities Act of 1933: II*, 8 Fortune 53, 108, states, referring to Section 11 of the Act "The rights against those responsible for the registration statement run in favor of all innocent buyers whether or not the purchase is made by the use of the mails or through channels of interstate commerce." We have found no similar statement in the article concerning the requirements of Section 12(2) with respect to the use of the mails.

[7] Dean, *The Federal Securities Act: I*, 8 Fortune 50 (1933).

[8] Douglas and Bates, *The Federal Securities Act of 1933*, 43 Yale L. J. 171 (1933), at page 183 in footnote 51 contains the following:

> "Civil liability under Section 12 would *probably* follow even though only part of the entire transaction was consummated in interstate commerce or through the mails. Thus solicitation of the sale through the mails or by interstate commerce followed by delivery of the security in a wholly intrastate transaction without use of the mails would probably be sufficient, *and vice versa*." (Emphasis supplied)

II. TEXAS LAW IS ADEQUATE TO PROTECT PURCHASERS.

The amicus curiae and the respondent both seem to be of the opinion, for different reasons, (*Cf.* Amicus Br., pp. 18, 19 with Resp. Br., pp. 20-22) that the Texas statute is not adequate to protect investors within the State. We assume that if this were the case it would under our federal system be a question concerning only the State of Texas and its citizens, such as petitioners and respondents here. We point out, however, that so far as the present case is concerned the complaint alleges affirmative misrepresentations and seeks a remedy i.e., cancellation and rescission, which concededly is available under the Texas securities law. Indeed, the present complaint alleges injury "both as a result of . . . violation of the Securities Act of 1933 and under the statutes of the State of Texas" (R. 15) and the same relief is requested against the same parties under the Securities Act of 1933 or "in the alternative" . . . "under the laws of the State of Texas" (R. 15-16). This prayer was of course refused by the District Court (R. 45).

We have also seen complaints filed by respondents' counsel in the state courts of Texas on behalf of other plaintiffs against other defendants but including also petitioners. The relief sought and the allegation in those complaints are almost identical with the allegations in the present complaint except for those few changes necessary to allege the existence of a security.[9]

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[9] See, e.g., *Schoon* v. *Bentsen, et al.*, No. B-17576, in the 93rd Dist. Ct. of Hidalgo County, Texas; *Whitson* v. *Bentsen, et al.*, No. B-18214 in the same court; *Bertelson* v. *Bentsen, et al.*, No. B-18327 in the same court, and *Meyer* v. *Bentsen*, No. A-8286, in the 92d District Court of Hidalgo County, Texas. Certified copies of these complaints will be lodged with the Clerk of this Court.

This disposes of respondents' argument that under Texas law a buyer cannot sue a person controlling the seller. (Rep. Br. pp. 20, 21)[10]

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There is so much mention by respondents of matters outside the record that we feel that a brief statement may be helpful in explaining to the Court the events which led to these actions. This is one of a series of similar lawsuits brought by the same counsel on behalf of different plaintiffs against different defendants. It was the first one to allege violation of federal law, the other actions being based on state law. The background facts are as follows:

The petitioners (the Bentsens) had for many years been in the business of sell real estate in the Rio Grande Valley. In connection with the sales of real estate, care contracts were frequently entered into. Some years ago for personal reasons the Bentsens retired from the real estate business although they still owned a good deal of acreage. A number of persons who had experience in real estate formed companies of their own to sell in the area. The Pummills, defendants in the present action, were one such group. There were many others, some of whom had been in business previously. The Bentsens sold land to these persons partly on credit, retaining a vendors lien to protect their rights. Each company conducted independent sales from the land which they had purchased from the Bentsens.

In January 1951 there was an unprecedented freeze in the Rio Grande Valley which destroyed approximately 80% of the citrus trees in the valley. Thereafter many purchasers came to the conclusion that the land

[10] In fact petitioners were not in control of the sellers. But respondents are equally free to allege that petitioners are liable under state or federal law, and equally unable to prove it in either case.

they purchased had been sold to them by misrepresentation. Counsel for respondents here were retained by a number of such purchasers from within and without the state. Actions were commenced against the defendants in the present action, the Pummills, and against other groups that had sold other pieces of land. The allegations were substantially parallel in all cases. In a number of these actions, stated by respondent to be twenty-five (Br. p. 21 n. 9), the Bentsen petitioners were joined on the theory that their vendors lien made them conspirators. As the respondents themselves indicate, almost all these actions were commenced in reliance on State law.

III. THE USE OF THE MAILS HERE IS NOT PART OF THE SALE.

The amicus and respondents argue that the delivery of the deeds and care contracts by mail is part of the sale and not a delivery after sale. This misconceives the nature of securities transactions and the nature of the present transaction. The complaint alleges (we believe contrary to the fact) that the transactions here involved are securities transactions. If so, it is concededly (Amicus Br. p. 6, 7) only because the Securities Act defines "security" to include an "investment contract". This Court in *SEC* v. *W. J. Howey Co.*, 328 U.S. 293, 298, 299, stated:

> "In other words, an investment contract for purposes of the Securities Act means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise."

The Court then held the sale of land and a care contract (there called a service contract) jointly amounted to an investment contract and that the respective shares in the common enterprise "are evidenced by land sales contracts

and warranty deeds, which serve as a convenient method of determining the investors' allocable share of the profits. The resulting transfer of rights in land is purely incidental." *Id.* 300.

Under this language, the investment contract is created and paid for in the face to face transaction in Hidalgo County, Texas. What follows thereafter is merely transmission of evidence of what has already taken place. It is not part of the sale. In securities parlance and the language of the statute (§ 5(a)(2), 5(b)(2), 15 U.S.C. § 77e(a)(2) and 77e(b)(2)), it is part of the process of "delivery after sale." Accordingly, the delivery of the deed, after recordation, through the mails and the transmission of the previously executed care contract through the mails was merely a delivery of evidences of what has already occurred.

Had they not been sent through the mails to the purchasers the status of the parties would have been the same. Amicus suggests (page 38, n. 38) that under Texas law delivery of a deed is necessary to pass title. This is true but it is also well established under Texas law that delivery of the deed occurred when the grantor had it recorded in the purchaser's name. See e.g., *Ford* v. *Hackel*, 124 Tex. 402, 77 SW 2d 1043 (1935); *Caldwell* v. *Tucker*, 246 SW 2d 923 (Tex. Civ. App. 1952). Plainly therefore the title deeds had been effectively "delivered" to the purchasers under Texas law before the mailing of the copies with notice of recordation upon which the complaint relies.

Translated to terms of the normal securities transaction the analogy is as follows:

A customer in a brokerage office in New York agrees to buy certain shares and pays for them. He receives immediately a confirmation that the brokerage firm has sold him so many shares at such and such a price and that payment has been received. The security is in such case normally not delivered for several days. It may be necessary to obtain signatures on the certificates to authorize

transfer . It may be necessary to register the shares in the purchaser's name (see the analogy of recordation of the deeds in the present case); it may be desired by the purchaser to have the shares in specific denominations which may not be readily available. These procedures take a few days and then the shares are sent to the purchaser, normally by registered mail.

The "sale" is concluded in the face to face transaction. What occurs thereafter is a mere incidental mechanical process described properly as delivery after sale.[11]

Such transactions in securities occur daily in all the financial centers of the United States. They are of the type which are in all aspects local, where purchaser and seller reside in the same community and where state law is adequate to protect the investor. To hold that the incidental delivery of securities after sale which takes place almost universally by mail is part of the sale and a ground for federal jurisdiction in civil actions would make the Securities Act the governing law in every local securities transaction.

IV. MISCELLANEOUS POINTS

a. The Care Statement Is Not a Basis for Jurisdiction.

It is argued by respondents here that statements for expenditures for care are parts of the sale of the security and that the care statements are "in the nature of prospectuses" (Resp. Br. p. 16).

The court below did not rely on these care statements restricting itself in its opinion to "delivery of the deeds and contracts". Nor does amicus support this position.

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[11] Cf. the published opinion of the General Counsel of the Securities and Exchange Commission that a securities transaction is completed "when the customer parts with value in connection with the transaction". Securities Exchange Act Release No. 253, May 31, 1953. This relates to Section 11(d)(2) of the Securities Exchange Act, 15 USC § 78k(d)(2) requiring confirmation "at or before the completion of the transaction".

It will be remembered that the care statements arose in the following manner. Under the care contract the purchaser set up a fund in a bank in Hidalgo County, Texas, upon which the care company, i.e., the Pummill Management Company, could draw. Monthly the management company sent the purchaser a statement of the funds which it had drawn and the purposes for which the funds had been expended. The purchaser under its care agreement was then obligated to replenish the deposit. These care statements were mere statements of expenditures. They were not as respondent states "in the nature of prospectuses" since a prospectus is defined in the Act as a communication "which offers a security for sale" Section 2(10).

The "investment contract" as we have seen had been previously created and "sold". The argument of respondent attempts to confuse the sale with subsequent transactions, under an analysis which would make the sale of the investment contract here a five year process (Resp. Br. p. 18)! Such a contention cannot be sustained in the light of the fact that the "investment contract" was as we have seen created and sold in the face to face transaction.

Indeed, the complaint makes this abundantly clear. For example, uniformly it is alleged that a particular plaintiff "did on February 24, 1950 purchase said securities and/or investment contracts . . ." The next sentence of the complaint begins "That *since the date of said purchase,* said Plaintiff has spent" an additional sum for care of the trees. See R. 3, 5, 6, 7, 8, 8-9, 9. This formulation is followed in every paragraph of the charging count (R. 3-10). It is then followed by a recitation (R. 10, 11) of the alleged misrepresentations but for which it is alleged, the respondents

"would not have made said investment." It then alleges that "after" the making of the investment the mails were used to forward the deeds, contracts and statements and that then the defendants "continued to make false representations by sending to Plaintiffs, through the United States mails, various care bills including therein charges for irrigation water which was neither used nor available to the Defendants for such use" (R. 11, 12).

The complaint clearly alleges that the "investment contract", was purchased and sold in each case on the specified date, and that the care statements were mailed only after the purchase and sale was completed.

b. Respondents Cannot Here Attempt to Argue That Section 17(a) Provides an Independent Basis for Civil Suit.

Respondents seek to argue that they have a civil remedy not only under Section 12(2) but also under Section 17(a) and that the language of Section 17(a) is broadly enough phrased to cover the situation even if Section 12(2) does not. We respectfully submit that this issue is not within the grant of the petition for certiorari, and that it was not even raised in the Court of Appeals. If so advised, the respondents if their complaint is stricken down by this Court, may seek to revive it by these desperate means in the District Court.

In any event, we point out how far fetched the respondents' contention is. It suggests that although Congress prescribed in specific terms a carefully defined remedy in Section 12(2) with specific relief and specified burdens of proof, it nevertheless in the same statute inadvertently created a different and independent remedy for the identi-

cal situation governed only by the law of illegal transactions.[12]

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March, 1954.

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[12] In this connection it should be noted that the statute of limitations (Section 13) was amended in 1934 to cut the period of limitations for action under 12(2). Certainly Congress could not have believed that a remedy existed under Section 17 which would not be covered by this limitation provision.

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In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., ET AL., PETITIONERS

v.

EMERY C. BLACKWELL, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE SECURITIES AND EXCHANGE COMMISSION, AMICUS CURIAE

The Solicitor General submits this memorandum on behalf of the Securities and Exchange Commission, *amicus curiae*, with respect to the petition for a writ of certiorari filed herein.

The Commission participated as *amicus curiae* both in the District Court and in the Court of Appeals, and believes that the decision below is entirely correct. It recognizes, however, that on the sole question on which petitioners seek review—*viz.*, the proper construction of the clause in Section 12 (2) of the Securities Act of 1933 dealing with interstate commerce and the mails—the decision below conflicts with that of the Court

of Appeals for the Seventh Circuit in *Kemper* v. *Lohnes,* 173 F. 2d 44. While the Commission regards the *Kemper* decision as erroneous, in view of the conflict it does not oppose review limited to that single question.

The question presented arises on a motion to dismiss a complaint asserting fraudulent sales of "securities" in the nature of "investment contracts". The following is alleged: Petitioners control a purported citrus fruit development in the Rio Grande Valley of Texas in which respondents invested substantial sums of money (R. 21–24). Respondents are members of the investing public. They reside in other parts of Texas and had no familiarity with this citrus promotion other than that obtained from petitioners' salesmen (R. 3–4). Each of them was offered a unit or units of land in the development,[1] together with a "care contract" therefor. The promoters undertook, pursuant to the care contracts, to cultivate and develop these units on behalf of the investors, and to harvest and market the crop (R. 3, 17, 18, 46). They told prospective investors that "by investing in said Citrus Development * * * [they] could get in on an 800-acre unit which would be developed by one company in a uniform manner and under the management of citrus experts, for the joint benefit of all inves-

[1] A unit encompassed a 20-acre parcel priced at $400.00 per acre.

tors", and that the investors "would not have a thing to worry about" (R. 17–18). They represented that they "would take care of all the problems which might arise, and the investor would only have to sit back and reap the dividends" (R. 18). It was further represented that the property would be paying all of its expenses within three years, and that the "investment would produce a minimum of 20% per year return * * * after five years" (R. 17). To induce respondents to invest their moneys, numerous fraudulent misrepresentations were made as to the character, quality and value of the acreage, the available supply of water, the quality of citrus stock to be planted, the care and management to be provided, and the prospects of profits (R. 16–21). Respondents paid for their land parcels immediately—in cash or by a combination of cash and interest bearing vendor's lien notes. Payments on the care contracts, however, were placed on a periodic basis (R. 5–16). Each investor was required to deposit sufficient funds in a bank account held jointly with the promoters to meet the investor's financial commitments under the care contract (*ibid.*). The misrepresentations which induced the sales were made orally (R. 18); but the promoters used the mails to transmit the warranty deeds for the parcels of land, the care contracts, and the periodic billings or statements on said contracts (R. 19). The periodic billings

themselves, according to the complaint, contained further misrepresentations to deter withdrawals from the investment agreements (R. 18–19). After large sums of money had been obtained from public investors, the venture collapsed as the result of the lack of skilled labor and essential equipment, and of general neglect on the part of the promoters (R. 19–20). By the instant action, investors seek to obtain rescission or recover damages (R. 24–26).

Petitioners challenged the sufficiency of the complaint on a number of grounds which included (1) the failure to allege transactions describing sales of "securities" within the meaning of the Securities Act of 1933, and (2) the failure to allege that the mails were used to transmit the misrepresentations complained of so as to render applicable the civil liabilities provisions of Section 12 (2) of the Act (15 U. S. C. 77*l* (2)) (R. 26–30). Agreeing with petitioners on these two grounds, the District Court dismissed the complaint (R. 54–71). The Court of Appeals, however, rejected petitioners' contentions, reversed the District Court, and remanded the case for trial on the merits. *Blackwell* v. *Bentsen,* 203 F. 2d 690 (R. 81–87).

The Court of Appeals concluded that the transactions alleged fell well within the area of "investment contracts" delineated by this Court in *S. E. C.* v. *W. J. Howey Company,* 328 U. S.

293, and *S. E. C.* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344. It took cognizance of the *Kemper* decision in the Seventh Circuit on the mailings question, but refused to follow it. Instead, it followed the decision of the Court of Appeals for the Second Circuit in *Schillner* v. *H. Vaughan Clarke & Co.*, 134 F. 2d 875, and held that the alleged uses of the mails to transmit the deeds and care contracts to consummate the transactions were sufficient to afford jurisdiction under Section 12 (2).

While petitioners deny that there have been sales of securities and characterize the controversy as simply a "local land dispute", the position they take at this time is that—

> * * * this question is basically one of construction of the pleadings and we do not believe that it is of sufficient consequence to merit the attention of this Court under its rules. We therefore confine this petition to the error of the court below in holding that use of the mails for incidental delivery of the documents after sale is sufficient basis for federal jurisdiction under Section 12 (2) of the Securities Act of 1933. If it should be necessary after action by this Court, we shall present to the trial court, after evidence, the question of the existence of a security [Pet. 7].

In the Commission's view, there is no need for further review of the decision below as respects the "securities" question; and it would have opposed the grant of a writ of certiorari had it been

sought on that ground. The ruling below on that question is correct and presents no conflict with that of any other court.

As previously stated, the Commission believes that the court below also correctly decided that the alleged uses of the mails to consummate the transactions—*i. e.*, to deliver the documents evidencing the securities, and to obtain part of the purchase moneys—sufficed to bring the transaction under Section 12 (2). Insofar as pertinent that Section provides:

> Any person who * * * sells a security * * *, by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact * * * shall be liable to the person purchasing such security from him, * * *.

In light of the statutory purposes to outlaw fraudulent sales of securities and to provide civil remedies therefor to the extent that Congress was constitutionally able to do so,[2] and in the light of the many court decisions holding with unanimity

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[2] Cf. *Fratt* v. *Robinson*, 203 F. 2d 627, 635 (C. A. 9); *United States* v. *Monjar*, 47 F. Supp. 421, 425 (D. Del.), affirmed, 147 F. 2d 916 (C. A. 3), certiorari denied, 325 U. S. 859; *United States* v. *Kott*, 1 SEC Jud. Dec. 228, 229 (S. D. Tex.), reversed on other grounds, *sub nom. Seeman* v. *United States*, 90 F. 2d 88 (C. A. 5).

that these and similar uses of the mails are sufficient to invoke the other fraud provisions of the federal securities laws, including provisions giving rise to civil liabilities,[3] the court below properly concluded that the language in Section 12 (2), "by means of a prospectus or oral communication, which includes an untrue statement of a material fact" etc., refers to the opening clause, "sells a security" and does not modify the jurisdictional clause, "by the use of * * * the mails". To hold otherwise, as these petitioners suggest, would mean that there can be no civil recovery under Section 12 (2) of the Securities Act of 1933 for sales induced by fraudulent misrepresentations made orally, even though the very same conduct constitutes a criminal offense under Section 17 (a) of the statute.[4] It is inconceivable to

[3] See, e. g., *Fratt* v. *Robinson*, 203 F. 2d 627 (C. A. 9); *United States* v. *Earnhardt*, 153 F. 2d 472 (C. A. 7), certiorari denied, 328 U. S. 858; *Bogy* v. *United States*, 96 F. 2d 734 (C. A. 6), certiorari denied, 305 U. S. 608; *Slavin* v. *Germantown Fires Ins. Co.*, 174 F. 2d 799 (C. A. 3); *Northern Trust Co.* v. *Essaness Theatres Corp.*, 103 F. Supp. 954 (N. D. Ill.); *United States* v. *Vidaver*, 73 F. Supp. 382 (E. D. Va.).

[4] Section 17a (15 U. S. C. 77q (a)), provides:

> (a) It shall be unlawful for any person in the sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—
>
> (1) to employ any device, scheme, or artifice to defraud, or
>
> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order

us that Congress intended by the differently worded language of Section 12 (2) (occasioned by the difference in the remedy provided) to impose a more restricted field for civil recovery than that provided for criminal prosecutions. Nor is the text of Section 12 (2) susceptible of petitioners' construction, except possibly by the total disregard of the statutory context. Relevant legislative history, which was discussed in our brief below but upon which we do not elaborate at this time, also appears inconsistent with petitioners' proffered construction.

No analysis of the question was provided by the Court of Appeals for the Seventh Circuit in the *Kemper* opinion, which simply assumed that Section 12 (2) required that the mails be used to transmit the misrepresentations. This is true also of the earlier statement in *Siebenthaler* v. *Aircraft Accessories Corp.*, CCH Fed. Sec. L. Rep. ¶ 90,122 (W. D. Mo.),[5] and the prior dicta in two other cases upon which petitioners rely.[6] In

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to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

[5] The actual holding in the *Siebenthaler* case is not clear. There is no positive finding of any fraudulent misrepresentation or omission.

[6] In *Murphy* v. *Cady*, 30 F. Supp. 466 (D. Maine), affirmed, 113 F. 2d 988 (C. A. 1), plaintiff recovered on proof of oral misrepresentations communicated by interstate tele-

contrast, the decision below and that of the Court of Appeals for the Second Circuit in the *Schillner* case (134 F. 2d, at 877–8) are well reasoned. The Court of Appeals for the Ninth Circuit, in dealing with a comparable mailings question in a civil action for a fraudulent purchase of securities brought under the companion anti-fraud provisions of Rule X–10B–5, 17 C. F. R. 240.10b–5, promulgated pursuant to Section 10 (b) of the Securities Exchange Act of 1934, 15 U. S. C. 78j (b), gave consideration to the related question under Section 12 (2) of the Securities Act of 1933, and agreed with the court below that the *Schillner* decision contained "the best reasoning". *Fratt* v. *Robinson*, 203 F. 2d 627, at 634, n. 20. See also *Moore* v. *Gorman*, 75 F. Supp. 453 (S. D. N. Y.).

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phone. Similarly, in *Independence Shares Corp.* v. *Deckert*, 108 F. 2d 51 (C. A. 3), reversed without discussion of point, 311 U. S. 282, the alleged misrepresentations were transmitted by the use of federal instrumentalities. At a later stage of the proceedings the court observed that "The gravamen of the cause of action * * * is the misleading of the purchaser." *Pennsylvania Co.* v. *Deckert*, 123 F. 2d 979, 984. *Gross* v. *Independence Shares Corp.*, 36 F. Supp. 541 (E. D. Pa.), which petitioners also cite, contains nothing specific on the question. Indeed, the court held that the mailing of payment notices and other material designed to induce investors to continue contracts relating to securities sold under an installment payment plan was sufficient. It should be observed that, in the present case, the complaint similarly alleges that the periodic billings on the care contracts contained misrepresentations intended to deter respondents from terminating their investment arrangements.

The Commission was not a participant in the *Kemper* and other cases relied upon by petitioners.

As previously indicated, the Commission does not oppose the grant of a writ of certiorari on the question as to the requisite use of the mails under Section 12 (2) of the Act. However, since the decision below is correct and since the ruling in the *Kemper* case has not been followed, we have not deemed it appropriate to urge affirmatively that the ruling below on that question be reviewed.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 423

LLOYD M. BENTSEN, SR., ET AL., PETITIONERS

v.

EMERY C. BLACKWELL, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION, AMICUS CURIAE

OPINIONS BELOW

The opinion of the Court of Appeals (R. 50-54) is reported in 203 F. 2d 690. The opinion of the District Court (R. 34-46) is not reported.

JURISDICTION

The judgment of the Court of Appeals was entered on April 27, 1953 (R. 55). Petitions for rehearing were denied on July 27, 1953 (*ibid.*). The petition for writ of certiorari was filed on October 21, 1953, and granted on December 7, 1953 (R. 56, 346 U. S. 908). The jurisdiction of this Court is invoked under 28 U. S. C. 1254. See also

Section 22(a) of the Securities Act of 1933, 15 U.S.C. 77v (a).

QUESTIONS PRESENTED

1. Whether, under Section 12(2) of the Securities Act of 1933, a purchaser of securities may recover for oral misrepresentations made face to face where the sale was later consummated by use of the mails.

2. Whether the allegations of delivery through the mails of the deeds and contracts, essential parts of the investment contracts here involved, were sufficient to invoke jurisdiction under Section 12(2).

STATUTE INVOLVED

Section 12(2) of the Securities Act of 1933 (the "Act"), 48 Stat. 74, 15 U.S.C. 77l (2), provides:

> Any person who—
>
> * * * * *
>
> (2) sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not

sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

Section 17(a) of the Act, 15 U. S. C. 77q(a), provides:

(a) It shall be unlawful for any person in the sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Other statutory provisions are set forth in relevant part in the argument below where necessary.

STATEMENT

The questions presented arise on a motion to dismiss a complaint asserting causes of action under Section 12(2) of the Act for fraudulent sales of securities in the nature of investment contracts. The following facts are alleged in the complaint:

Petitioners control a purported citrus fruit development in the Rio Grande Valley of Texas in which respondents and other members of the buying public were induced to invest substantial sums of money (R. 13-15; 3-10). Respondents resided in other parts of Texas and had no familiarity with this promotion (R. 2).[1] Each respondent was offered a unit or units of land in the development, together with a "care contract" therefor.[2] The promoters[3] undertook, pursuant to the care con-

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[1] While the respondents in this case are alleged to be residents of Texas, petitioners' brief discloses that residents of other states were induced to invest money in the promotion. Thus, petitioners refer to "out of state plaintiffs" in other actions in the federal courts based on "diversity of citizenship" apparently involving the same promotion (Pet. Br. 16).

[2] A unit encompassed a 20-acre parcel priced at $400.00 an acre.

An issue, which is not material here, exists as to whether two of the complainants entered into care contracts (R. 29, 53).

[3] The action was brought against the following defendants: Pummill Development Company, the corporate vendor of the land units; Pummill Management Company, an affiliate which handled the care contracts; Earl and Carl Pummill, directors and stockholders of the foregoing companies; petitioners Lloyd M. Bentsen, Sr., Elmer C. Bentsen, and their firm, Bentsen Development Company, who allegedly controlled the Pummills and the over-all operations of the promotion; and certain other individuals who allegedly participated in the transactions as agents, employees, or co-conspirators (R. 1, 13-15). Defendants, other than the instant petitioners, did not seek a writ of certiorari.

tracts, to cultivate and develop these units on behalf of the investors, and to harvest and market the crop (R. 10-11; 29-33). They told prospective investors that "by investing in said Citrus Development * * * [they] could get in on an 800-acre unit which would be developed by one company in a uniform manner and under the management of citrus experts, for the joint benefit of all investors", and that the investors "would not have a thing to worry about" (R. 10-11). They represented that they "would take care of all the problems which might arise, and the investor would only have to sit back and reap the dividends" (R. 11). It was further represented that the property would be paying all of its expenses within three years, and that the "investment would produce a minimum of 20% per year return * * * after five years" (R. 10-11).

To induce respondents to invest, fraudulent misrepresentations and misleading omissions of material facts were made as to the character, quality, and value of the acreage, the available supply of water, the quality of citrus stock to be planted, the care and management to be provided, and the prospects of profits (R. 10-13). Respondents paid for their land parcels in cash or by a combination of cash and interest-bearing vendor's lien notes. Payments on the care contracts, however, were placed on a periodic basis. (R. 3-10.) In this connection, each investor was required to deposit from time to time in a bank account held jointly with the promoters sufficient funds to meet his

financial commitments under the care contract (*ibid.*).

The misrepresentations which induced investors to enter into the investment contracts were made orally (R. 11); but the promoters used the mails to transmit the warranty deeds for the parcels of land, the care contracts, which bore dates later than those on the deeds, and the periodic billings or statements on said contracts (R. 11-12).[4] The periodic billings themselves, according to the complaint, contained further misrepresentations to induce continued payments under the investment arrangements and to deter withdrawals therefrom (R. 12). After large sums of money had been obtained from public investors, respondents discovered that the venture was doomed to failure because of the lack of suitable water, skilled labor and essential equipment, and general neglect and abandonment on the part of the promoters (R. 12-13). By the instant action, investors seek to obtain rescission or recover damages (R. 15-16).

Petitioners and others named as defendants challenged the sufficiency of the complaint on a number of grounds including: (1) a failure to allege sales of "securities"—"investment contracts" in this case—within the meaning of the Act; and (2), a failure to allege that the mails were used to transmit the particular misrepresentations complained of, which, they contended, was necessary to render

[4] The petitioners' statement (Pet. Br. 5) that the deeds were mailed only after being recorded in the investors' names goes beyond the complaint and, in any event, is immaterial here. See pp. 37-38, *infra*.

applicable the civil liabilities provisions of Section 12(2) (R. 16-19, 23). Agreeing with the defendants on these two grounds, the District Court dismissed the complaint (R. 34-46). The Court of Appeals, however, rejected both contentions, reversed the District Court, and remanded the case for trial on the merits (R. 50-54).

The Court of Appeals concluded that the interests sold fell well within the area of "investment contracts" delineated by this Court in *S. E. C.* v. *W. J. Howey Company,* 328 U. S. 293, and *S. E. C.* v. *C. M. Joiner Leasing Corp.,* 320 U. S 344 (R. 52-54). It held, further, that the alleged uses of the mails to transmit the deeds and care contracts to consummate the transactions were sufficient to bring the sales within the scope of Section 12(2) (R. 54).

Petitioners sought a writ of certiorari "confine[d] * * * to the error of the court below in holding that use of the mails for incidental delivery of documents after sale is sufficient basis for federal jurisdiction under Section 12(2) of the Securities Act of 1933" (Petition, p. 7). Petitioners also expressed disagreement with the Court of Appeals that there had been sales of securities and sought to characterize the controversy as simply a "local land dispute", but stated that certiorari was not sought on that ground. Although their brief on the merits contains similar references to "local land disputes", the argument is confined to the ruling below on the sufficiency of the use of the mails.

The Securities and Exchange Commission, as *amicus curiae,* filed briefs in both courts below expressing agreement with the views which the Court of Appeals subsequently adopted. The Commission also filed, as *amicus curiae,* a memorandum on the petition for certiorari. It did not oppose review of the ruling on the sufficiency of the uses of the mails in light of the conflict with an earlier holding of the Court of Appeals for the Seventh Circuit in *Kemper* v. *Lohnes,* 173 F. 2d 44 — a holding which the Commission regards as clearly erroneous and which the court below declined to follow.

SUMMARY OF ARGUMENT

The court below correctly decided that the alleged use of the mails to consummate the sales by delivery of the deeds and care contracts sufficed to bring the transactions within the provisions of Section 12(2) of the Securities Act of 1933.

I

Both the text and context of Section 12(2) lead to the conclusion that the cause of action afforded by that section is not dependent upon use of the mails or facilities of interstate commerce to transmit the misrepresentations, and that a mailing elsewhere in the sale transaction is sufficient.

As a matter of grammar, the third phrase "by means of a prospectus or oral communication, which includes an untrue statement of a material fact," modifies solely "sells a security" and is not merely an extension of the second phrase "by the

use of any means or instruments of transportation or communication in interstate commerce or of the mails." The language "sells * * * by the use of any means * * * of *transportation* or communication * * *," and the broad preamble reference to "securities sold * * * through the mails," further negate petitioners' contention that there must be fraudulent communication by use of one of the stated instrumentalities.

The correctness of the above construction is shown also by the statutory context. The civil recovery provisions of Section 12(2) are but part of an integrated program designed to obtain informed and honest dealings in securities. The registration provisions of the Act require disclosure of pertinent information in connection with offerings to the public so that an investor may have an opportunity to exercise an informed judgment. Other provisions of the Act, including Section 12(2), are designed to curb fraud and deception in the sale of securities generally. Section 17(a) renders fraudulent and deceptive sales unlawful, and Section 12(2) authorizes civil recovery. While Congress has deemed it appropriate to exempt certain securities and transactions from the registration requirements of the Act, it has expressly provided that there are to be no exemptions from the antifraud provisions of Section 17(a), and but one exemption, not material here, from the civil recovery provisions of Section 12(2). Thus, the exemption from registration afforded for purely intrastate sales of securities locally issued is not available

under the provisions of Sections 12(2) and 17(a) which are designed to curb fraud. Congress, of course, has power to legislate with respect to intrastate uses of the mails; and petitioners do not deny that it has made unlawful under Section 17 (a) the use of the mails in a fraudulent sale of securities whether or not such use involves the transmission of the misrepresentations complained of. Section 12(2), which is the civil recovery counterpart of Section 17(a), was clearly intended to have the same broad scope.

The legislative history shows that the provisions relating to the uses of the stated federal instrumentalities were intended to afford constitutional support for the broad program adopted, and that Congress intended to make *full use* of its constitutional powers to achieve, through Section 12(2) as well as other provisions, the remedial objectives of the legislation.

Petitioners' proffered construction, based on a strained reading of Section 12(2), would frustrate the remedial purposes of the statute and lead to absurd and wholly incongruous results. It would deprive public investors of the benefits of the civil action provided by Section 12(2) in the case of oral misrepresentations, except in instances such as those involving a conversation across a state line or one over an interstate telephone. Under petitioners' interpretation, a fraudulent promoter could use the mails in selling securities to public investors, but yet avoid civil liability under Sec-

tion 12(2) by making his representations orally rather than in writing. Petitioners' construction would also mean that no civil liability would accrue under Section 12(2) for "face to face" misrepresentations in the sale of securities even though, as petitioners concede, the very same conduct violates Section 17(a) and is a criminal offense, and even though such misrepresentations if made in the *purchase* of the securities, rather than in the sale, would enable the defrauded seller to obtain civil recovery pursuant to the companion anti-fraud provisions of Rule X-10B-5 under Section 10(b) of the Securities Exchange Act of 1934. Moreover, contrary to petitioners' assertion, the relegation of investors to the remedies available at common law or under state statutes would cause them to lose important rights. Section 12(2) accords a defrauded investor a more simple and effective right of action than that given by the common law; and provides many advantages not afforded by the Texas Securities Act to which petitioners refer.

All but one of the actual court holdings support the view that the misrepresentations need not be communicated through interstate facilities or the mails if either instrumentality has been, or is later, used elsewhere in the sale transaction. The one court of appeals' ruling to the contrary, and a few other cases containing language which paraphrases Section 12(2) restrictively, offer no analysis of the statutory considerations and are entitled to little weight.

II

The alleged uses of the mails to deliver the deeds and care contracts—essential parts of the investment contracts—were mailings in the sale of the securities within the ambit of Section 12(2). Petitioners' suggestion that delivery of the documents is not part of the sales transaction because it confers no additional rights lacks merit as a general proposition and, moreover, ignores allegations in the complaint to the effect that the care contracts, at least, were not completed until the delivery.

The basic statutory definition of "sale" and "sell" includes a "disposition of * * * a security * * * for value" (Sec. 2(3)). The companion anti-fraud provisions of Section 17(a) and Rule X-10B-5 have been uniformly construed to apply where the mails have been used to deliver the securities even after the contract has been completed. This has also been the construction of Section 12(2) by the courts which have held sufficient under that section, too, use of the mails at any point in the sale of the security. An early district court statement to the contrary gave no consideration to the statutory definition, but relied instead upon particular language in the special context of the registration provisions of Section 5(a)(2). That statement, however, has since been rejected by other courts which have construed Section 12(2) in the light of the purpose of the Act.

ARGUMENT

I. Civil Recovery under Section 12(2) of the Securities Act of 1933 Is Not Dependent upon Use of the Mails to Transmit the Misrepresentations, it Being Sufficient that the Mails Were Used Elsewhere in the Sale Transaction.

The controversy relates to the proper construction of the first three clauses or phrases of Section 12(2) which, for purposes of this discussion, are separated in the excerpt set forth below:

> Any person who * * * sells a security * * *,
>
> by the use of any means or instruments of transportation or communication in interstate commerce or of the mails,
>
> by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading * * *
>
> shall be liable to the person purchasing such security from him * * *.

Under the construction adopted by the court below, clauses two and three independently modify "sells a security." As a matter of grammar, this is warranted by the comma between these two clauses, by the absence of qualifying language, and by the commencement of both clauses two and three with the preposition "by" which indicates that each was intended independently to modify the initial verb.

Petitioners urge, however, that clauses two and three should be read as a single phrase as though the comma were omitted, or as if the language of the section were inverted as follows:

> Any person who * * * sells a security * * * by means of a prospectus or oral communication * * * [transmitted] by the use of any means or instruments of transportation or communication in interstate commerce or of the mails shall be liable to the person purchasing such security from him * * *.

Petitioners' construction strains the language of Section 12(2); but if there is doubt as to the correctness of our reading of the section it can readily be resolved by consideration of the purpose of the provision, its history, and reference to the parallel provisions of the Securities Act and the Securities Exchange Act. Petitioners' intepretation goes a long way towards frustrating the remedial objectives of the Act. Thus, it would deprive public investors of the benefits of the civil recovery provisions of the Act where the misrepresentations have been oral, except in instances such as interstate telephone conversations or conversations across state lines. It would mean that civil recovery under the statute would not be available for "face to face" misrepresentations in the sale of securities to public investors even though, as petitioners do not deny (Pet. Br. 14-15), the very same conduct by the fraudulent seller is a criminal offense under Sections 17(a) and 24 of the Act, and even though such misrepresentations give rise to civil liabilities

under the companion anti-fraud provisions of Section 10 (b) of the Securities Exchange Act of 1934 (15 U.S.C. 78j(b)) and the regulations issued thereunder, if made in the *purchase*, rather than in the sale, of securities (see *infra*, pp. 23-26). The construction urged by petitioners has been expressly rejected by two courts of appeals [5] and disapproved by a third in a reasoned dictum. [6] It has been upheld by only one court of appeals which assumed the construction without discussion of the underlying statutory considerations. [7] These and other cases are discussed *infra*, pp. 33-37.

In construing Section 12(2), consideration should be given not only to the bare text, but also to the purpose of that section and its relationship to the other provisions of the Act. As this Court has emphasized, it is necessary to read "text in the light of context and [to] interpret the text so far as the meaning of the words fairly permits so as to carry out in particular cases the generally expressed legislative policy." [8]

The civil liabilities provisions of Section 12(2) are but part of a broad integrated program designed to obtain "honest dealing in securities." [9] The program has two major aspects: one relates to disclosure of pertinent information in connection with new offerings of securities to the public so

[5] The ruling below in the Fifth Circuit, and that in *Schillner* v. *H. Vaughan Clarke & Co.*, 134 F. 2d 875, in the Second Circuit.

[6] *Fratt* v. *Robinson*, 203 F. 2d 627, 634, in the Ninth Circuit.

[7] *Kemper* v. *Lohnes*, 173 F. 2d 44, in the Seventh Circuit.

[8] *S.E.C.* v. *C. M. Joiner Leasing Corp.*, 320 U.S. 344, 351.

[9] H. Rep. No. 85, 73d Cong., 1st Sess., p. 2 (1933).

that investors may have an opportunity to exercise an informed judgment; the other, which applies not only to new offerings but to sales generally, is designed to curb fraud and deception by imposing liability, both civil and criminal, for misrepresentations.

As respects the first of these, before an issue of securities may lawfully be offered to the public full disclosure of all material facts must be made pursuant to the registration provisions of the Act. Sections 5, 6, 7, 8, 10, 15 U.S.C. 77e, 77f, 77g, 77h, 77j. Exemptions from the registration requirements are provided with respect to certain securities and securities transactions which Congress, considering the interests of public investors and other factors, did not deem necessary to subject to those requirements. Sections 3(a), 4, 15 U.S.C. 77c(a), 77d. In addition, the Commission is given discretionary power to exempt from registration any public offering of securities where the aggregate amount of the issue does not exceed $300,000, Section 3(b), 15 U.S.C. 77c(b); and pursuant to Section 3(b) the Commission has issued appropriate regulations conditioning the exemption upon the filing of certain information with respect to such issues. See, *e.g.*, Regulation A, 17 C.F.R. 230.215 *et seq.* (18 Fed. Reg. 1434). Violations of these as well as other provisions of the Act, or the Commission's rules or regulations thereunder, may be enjoined by the Commission, Section 20(b), 15 U.S.C. 77t(b), and, if willfully committed, may give rise to criminal prosecution, Section 24, 15 U.S.C. 77x. Civil liability

for selling a security without complying with the registration requirements of the Act is provided by Section 12(1), 15 U.S.C. 77l(1). Misrepresentations or omissions of material facts in registration statements which have become effective under the Act give rise to civil liabilities under Section 11, 15 U.S.C. 77k.

The legislative program against fraud and deception in the sale of securities generally, however, is broader. Sections 17 and 12(2) of the Act, 15 U.S.C. 77q, 77l(2), respectively render unlawful, and authorize civil recovery for, fraud and misrepresentation in the sale of securities even with respect to securities and securities transactions which are exempted from the registration requirements. Thus, it is expressly provided in subparagraph (c) of Section 17 that the exemptions from other provisions of the Act shall not be applicable as respects the broad prohibitions of that section. Similarly, Section 12(2), with one exception not material here, [10] expressly renders those exemptions inapplicable as respects the corresponding broad civil liabilities provisions. For example, Congress has seen fit to exempt from the registration requirements purely intrastate sales of securities locally issued; [11] but such sales are clearly subject to the

[10] The sole exception is for government and bank securities exempted from the statute by Section 3(a)(2), 15 U.S.C. 77c(a)(2).

[11] Section 3(a)(11), 15 U.S.C. 77c(a), provides:

> Except as hereinafter expressly provided, the provisions of this title shall not apply to any of the following classes of securities:
>
> * * * * *

(Cont'd next page)

prohibitions of Section 17 against fraud and the provisions of Section 12(2) for civil recovery. The considerations which led Congress to exempt such purely intrastate transactions from the burden and expense of the federal registration requirements obviously were not regarded as sufficiently persuasive to warrant similar exemption from the broad statutory program against fraud and misrepresentation. Here is clear statutory negation of the argument, and innuendo, which pervade petitioners' brief that Congress did not intend to deal with fraud in the field of intrastate sales of securities.

The "statutory policy" has been described by this Court as that "of affording broad protection to investors." *S.E.C.* v. *W. J. Howey Co.*, 328 U. S. 293, 301. To effectuate this policy, Section 12 (2) affords an investor a more simple and effective right of action than that available at common law. *Wilko* v. *Swan*, 346 U. S. 427, 431.[12] The civil

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([11]) Any security which is a part of an issue sold only to persons resident within a single State or Territory, where the issuer of such security is a person resident and doing business within, or, if a corporation, incorporated by and doing business within, such State or Territory.

[12] In holding that the special court remedy afforded by Section 12(2) may not be waived by a pre-sale stipulation for arbitration obtained by the seller, the Court observed that the Securities Act "added to the ancient rule of *caveat emptor* the further doctrine of 'let the seller also beware' • • • " "Section 12(2)," the Court noted, "created a special right to recover for misrepresentation which differs substantially from the common-law action in that the seller is made to assume the burden of proving lack of scienter. The Act's special right is enforceable in any court of competent jurisdiction—federal

liability provision of the Texas Securities Act (Vernon's Tex. Rev. Civ. Stat. Ann., Art. 600a, § 33a) which petitioners cite (Pet. Br. 15) is hardly "substantially equivalent" (Pet. Br. 16) to Section 12(2); for rescission alone is authorized upon tender of the securities and the income received therefrom, and then for affirmative misrepresentations only, and the procedural advantages of Section 12(2) are not afforded.

With this background, we turn to a more detailed consideration of the provisions relating to the use of interstate instrumentalities or of the mails. The constitutional bases for the legislation, of course, are the power of Congress to regulate interstate commerce (Art. I, Sec. 8, Cl. 3) and its power with respect to the use of the mails (Art. I, Sec. 8, Cl.

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or state—and removal from a state court is prohibited. If suit be brought in a federal court, the purchaser has a wide choice of venue, the privilege of nation-wide service of process and the jurisdictional $3,000 requirement of diversity cases is inapplicable." (*Ibid.*)

See also Frankfurter, *The Federal Securities Act: II*, 8 Fortune 53, 108 (August, 1933):

> For willful violations of the Act there are, of course, criminal penalties. American legislative history, however, proves the very limited function of the criminal law in the assimilation by business of standards of public responsibility. The real needs are the building up of new business habits and the generation of a new moral climate for business. * * * *But an indispensable spur to observance of the standards of the Act is the right of recovery by the victims of disobedience.* * * * *The Act would be merely a pious resolution unless the standards of responsibility for the conduct of the investing business had the sanctions of rigorous civil liability.* [Emphasis supplied.]

7).[13] Federal power with respect to the mails is independent of the power relating to interstate commerce;[14] and, accordingly, it has been held that a purely intrastate mailing suffices to provide jurisdiction under the Securities Act of 1933. *Shaw* v. *United States,* 131 F. 2d 476 (C.A. 9); *Holmes* v. *United States,* 134 F. 2d 125 (C.A. 8), certiorari denied, 319 U.S. 776; *Hunt* v. *Securities and Exchange Commission,* 158 F. 2d 981 (C.A. 9); *Gross* v. *Independence Shares Corp.,* 36 F. Supp. 541 (E.D. Pa.). This the petitioners admit (Pet. Br. 24); nor do they challenge the power of Congress to authorize civil recovery for fraudulent sales of securities in which the mails have been employed, even though the misrepresentations may not have been transmitted through that federal instrumentality. In fact petitioners recognize that Section 17—the injunctive and criminal counterpart of Section 12(2)—has been uniformly construed to apply whenever the mails are used in connection with any part of the transaction (see pages 23-24, *infra*). But Section 17(a), petitioners suggest, is "perhaps more broadly phrased" (Pet. Br. 8). Section 12(2), however, petitioners contend, is limited by the statutory language itself to "a par-

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[13] Petitioners' argument that the postal power was included merely to back up a possibly invalid exercise of the interstate commerce power, apart from the fact that it is wholly beside the point since the use of the mails was included as a basis for jurisdiction whatever the motive, is somewhat disingenuous in light of the prior application of the mail fraud statute to securities transactions.

[14] *Badders* v. *United States,* 240 U.S. 391; *In re Rapier,* 143 U.S. 110.

ticular kind of use of the mails" (Petition, p. 11). So the issue is narrowed to that of the intent of Congress.

It is pointed out above (pp. 13-14 *supra*), that petitioners' proffered construction of Section 12 (2) is unwarranted as a matter of simple grammatical construction. Also, petitioners overlook the use of the language "sells a security * * * by the use of any means or instruments of *transportation* or communication in interstate commerce or of the mails" (emphasis added). This would seem to negate petitioners' contention that Section 12 (2) was intended to apply only where there is fraudulent communication by means of one of the stated federal instrumentalities (Pet. Br. 14); for, on the face of the statute, it appears to have been contemplated that the use of a federal instrumentality for purposes of "transportation" as well as "communication", in connection with the fraudulent sale, would suffice to render the civil recovery provisions applicable. Petitioners also give no consideration to the preamble of the Act which refers to the purpose "To provide full and fair disclosure of the character of securities *sold* in interstate and foreign commerce and *through the mails,* and to *prevent frauds in the sale thereof,* and for other purposes" (emphasis added). 48 Stat. 74. In *Wilko* v. *Swan,* 346 U. S. 427, 431, n. 9, this Court referred, *inter alia,* to this language in discussing the broad remedial objectives of the statute—particularly those of Section 12(2).

Petitioners' construction would frustrate the

remedial objective of Section 12(2). As previously shown, that section is but part of a broader integrated statutory program against fraud and misrepresentation in the sale of securities—the part which authorizes civil recovery.[15] Prior to the Securities Act of 1933, securities frauds were dealt with federally on a somewhat limited basis under the mail fraud and conspiracy statutes, infractions of which gave rise to criminal liability.[16] The Securities Act has greater impact. It provides federal legislation tailored to the securities field. As previously noted, not only are there criminal sanctions for the violation of Section 17, but the Commission is authorized to enjoin a threatened violation,[17] and an investor may obtain private relief in an action for damages or rescission. Moreover, civil recovery may be had for material misstatements or half-truths which may or may not constitute "fraud". The Securities Act of 1933 not

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[15] See also the following observation of Representative Rayburn, Chairman of the House Committee which passed upon the bill which became the Securities Act: "It makes [the seller] responsible civilly if he sells stocks upon a misrepresentation; it makes him guilty of fraud and criminally liable if he sells it [sic] with misrepresentation and fraudulent intent." 77 Cong. Rec. 2919.

[16] 18 U.S.C. 371, 1341. The mail fraud statute imposes criminal sanctions upon persons who, having devised or intending to devise a fraudulent scheme, "for the purpose of executing such scheme * * * or attempting so to do", use or cause the mails to be used. Clearly the misrepresentations need not be sent through the mails. *Pereira* v. *United States*, No. 50, this Term, decided February 1, 1954.

[17] Section 20(b), 15 U.S.C. 77t(b), authorizes injunctive relief against threatened violations of Section 17. Criminal penalties for willful violations are provided by Section 24, 15 U.S.C. 77x.

only goes far beyond the mail fraud statute in the securities field, but, for the most part, well beyond local law in dealing with misrepresentation and fraud in securities transactions. *Wilko* v. *Swan*, 346 U. S. 427, 430-31, 435, 438; *S.E.C.* v. *C.M. Joiner Leasing Corp.*, 320 U. S. 344, 353; *cf. S.E.C.* v. *W. J. Howey Co.*, 328 U. S. 293, 301. [18]

Section 17(a) (set forth in full at page 3, *supra*) is the counterpart of Section 12(2) in that it subjects the same type of fraud to Commission injunction or criminal prosecution. Subparagraph (2) of Section 17(a) makes unlawful the same misrepresentations and half-truths described in the civil recovery provisions of Section 12(2). The provisions of Section 17(a) as respects the requisite use of the mails or instrumentalities of interstate commerce are phrased a little differently than those of Section 12(2), apparently as the result of the difference in the type of legal action authorized. Section 17(a)(2) renders it "unlawful for any person in the sale of any securities * * * by the use of the mails, directly or indirectly * * * to obtain money or property by means of any untrue statement of material fact", etc. [19] Section

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[18] The mail fraud statute was not repealed by implication by the passage of the comprehensive provisions of the Securities Act of 1933. *Edwards* v. *United States*, 312 U. S. 473; *United States* v. *Rollnick*, 91 F. 2d 911 (C.A. 2).

[19] Section 17(b), on the other hand, clearly limits the prohibition of "touting", as distinguished from fraudulent "sales", to communications sent in interstate commerce or through the mails. Thus Congress knew how to draft provisions to achieve the limited construction urged by the petitioners when it desired to do so.

17(a), as the courts have held with unanimity, applies whenever the mails are used in the sale transaction, or in furtherance of the fraudulent scheme, irrespective of whether misrepresentations or half-truths have been transmitted through the mails.[20] "The character of the matter sent by mail is immaterial" where the mailing is connected with the fraudulent sale.[21]

Relevant also are the court decisions under Section 10 (b) of the companion Securities Exchange Act of 1934, 48 Stat. 881, 15 U.S.C. 78j(b). Section 10 (b) authorizes the Commission to promulgate rules rendering unlawful deceptive *purchases,* as well as deceptive sales, of securities. Pursuant to that section, the Commission has promulgated Rule X-10B-5 upon the pattern of Section 17 (a) of the Securities Act of 1933, but applicable to purchases

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[20] Examples of mailings held sufficient are: mailings of warranty deeds between defendants, and to the county clerk for recording and subsequent delivery to investors, *Mansfield* v. *United States,* 155 F. 2d 952 (C.A. 5), certiorari denied *sub nom. Browne* v. *United States,* 329 U. S. 792; mailings acknowledging part payment and transmitting deeds, *United States* v. *Earnhardt,* 153 F. 2d 472 (C.A. 7), certiorari denied, 328 U.S. 858; a mailing requesting delivery of securities to a third person and a reply by mail stating that this had been done, *Bogy* v. *United States,* 96 F. 2d 734 (C.A. 6), certiorari denied, 305 U. S. 608; mailings by defendants' agents to defendants containing reports relating to the execution of the fraudulent scheme and remitting bank drafts, *United States* v. *Monjar,* 47 F. Supp. 421 (D. Del.), affirmed, 147 F. 2d 916 (C. A. 3), certiorari denied, 325 U. S. 859; delivery of stock certificate after oral contract of sale and receipt of payment, *S.E.C.* v. *Wimer,* 75 F. Supp. 955 (W.D.Pa.); mailing by a bank to effect collection of a check representing the receipts of defendant's fraud, *United States* v. *Vidaver,* 73 Supp. 382 (E.D. Va.).

[21] *S.E.C.* v. *Timetrust, Inc.,* 28 F. Supp. 34, 42 (N.D. Calif.).

as well as sales.[22] In addition to providing a basis for governmental action by way of injunction or criminal prosecution,[23] the violation of Rule X-10B-5, as the courts have recognized, gives rise to a private cause of action for civil recovery in favor of a defrauded seller.[24] Rule X-10B-5, thus, constitutes another counterpart of Section 12(2) of the Securities Act in rounding out the program of

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[22] Rule X-10B-5, 17 C.F.R. 240.10b-5, provides:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security."

[23] See Sections 21(e) and 32 of the Securities Exchange Act of 1934, 15 U.S.C. 78u(e), 78ff.

[24] See, *e.g.*, *Fratt* v. *Robinson*, 203 F. 2d 627 (C.A. 9); *Fischman* v. *Raytheon Mfg. Co.*, 188 F. 2d 783 (C.A. 2); *Slavin* v. *Germantown Fire Ins. Co.*, 174 F. 2d 799 (C.A. 3); *Kardon* v. *National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa.); *Speed* v. *Transamerica Corp.*, 71 F. Supp. 457 (D. Del.), and 99 F. Supp. 808 (D. Del.); *Northern Trust Co.* v. *Essaness Theatres Corp.*, 103 F. Supp. 954 (N.D. Ill.). The right of action has been based on the tort doctrine that a person injured by another's violation of a statute intended for his protection may seek private relief if the statute does not withhold relief or make other provision for private relief inconsistent with the application of the tort doctrine, and upon the provisions of Section 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. 77cc(b), rendering void contracts made in violation of the statute or rules thereunder and containing other provisions consistent with the right of a defrauded seller to seek private recovery.

Congress. "The two Acts," it has been held, "are unquestionably in pari materia and must be construed together to make a consistent whole." *Rosenberg* v. *Globe Aircraft Corp.*, 80 F. Supp. 123, 124 (E.D. Pa.). Consistent with the construction given the mailings provision of Section 17(a) of the 1933 Act, it has been held that a seller may obtain civil recovery under Rule X-10B-5 for oral misrepresentations where the mails have been used at any point in connection with the fraudulent purchase. See, *e.g.*, *Fratt* v. *Robinson*, 203 F. 2d 627 (C.A. 9); *Northern Trust Co.* v. *Essaness Theatres Corp.*, 103 F. Supp. 954 (N.D. Ill.).

It has been recognized that the requirements in the anti-fraud provisions of these two statutes relating to the use of interstate commerce or the mails were not intended to set forth the gist of the offenses, but merely to establish the source of the power exercised by Congress to reach the interdicted fraud or deceit.[25] Stated differently, the "jurisdictional language" was intended to provide constitutional support for the broad statutory program adopted; and Congress intended to make full

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[25] See *Fratt* v. *Robinson*, 203 F. 2d 627, 635 (C.A. 9) ("* * * the use of the mails *per se* is not denounced, it is the fraud that offends. For that reason, it [the statute] denies the use of the mails in connection with the fraud."); *United States* v. *Monjar*, 47 F. Supp. 421, 425 (D. Del.), affirmed, 147 F. 2d 916 (C.A. 3), certiorari denied, 325 U. S. 859 ("The target at which the act aims is the scheme to defraud. True, use of the mails or the facilities of interstate commerce is the basis of federal jurisdiction"). See also *United States* v. *Kott*, 1 SEC Jud. Dec. 228, 229 (S.D. Tex.), reversed on other grounds, *Seeman* v. *United States*, 90 F. 2d 88 (C.A. 5); *cf. Kopald-Quinn & Co.* v. *United States*, 101 F. 2d 628, 632-33 (C.A. 5), certiorari denied, *sub nom. Ricebaum* v. *United States*, 307 U.S. 628.

use of its constitutional powers to achieve the remedial objectives of the legislation. It has already been shown that there has been no dissent from this view in the construction of the companion provisions of Section 17 (a) of the 1933 Act and Rule X-10B-5 under Section 10(b) of the 1934 Act; and, as we show more fully below, only one court of appeals has adopted a different view of the purpose of the "jurisdictional language" of Section 12(2). See pp. 33-36, *infra*. If the view of that court should prevail, the result would be that there could be no civil recovery under Section 12 (2) of the Securities Act of 1933 for sales induced by oral "face-to-face" fraudulent misrepresentation, even though the very same conduct could be enjoined or criminally prosecuted by virtue of Section 17 (a) of that Act, and even though the very same conduct on the part of a buyer of securities would afford a basis for civil recovery by the defrauded seller pursuant to Rule X-10B-5 under the companion Securities Exchange Act of 1934. For reasons previously stated, Section 12 (2) is not reasonably susceptible of such a construction. It is unlikely that Congress could have intended so incongruous a result. Surely a Congress aware of the fact that many securities frauds were induced by oral misrepresentations, and "trying to cover instances where there seem to be loopholes and means of escape" (77 Cong. Rec. 2983), did not intend to authorize easy evasion of a civil recovery provision deemed of paramount importance in preventing "further exploitation of the public by the

sale of unsound, fraudulent, and worthless securities through misrepresentation." S. Rep. No. 47, 73d Cong., 1st Sess. (1933), p. 1.

Petitioners' argument that the federal securities statutes were not intended to reach "local controversies"[26] is similar to the contention recently rejected by the Court of Appeals for the Ninth Circuit in *Fratt* v. *Robinson,* 203 F. 2d 627, where it had been urged that the companion anti-fraud provisions of Rule X-10B-5 promulgated pursuant to Section 10(b) of the 1934 Act could have no applicability to transactions in securities which had never been publicly traded on an exchange or in the over-the-counter market. Contrary to the view now urged by petitioners, that court held that the federal securities laws were intended to be of broad scope as respects fraudulent and deceptive transactions, and to reach, *inter alia,* intrastate and even private securities transactions involving use of the mails. Other federal courts have agreed with this construction.[27] Petitioners' professed concern that

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[26] It may be pertinent to recall that petitioners' repeated references to "local controversy" appear to be at variance with the disclosure in their own brief that many out of state residents were induced to invest in the promotion and have instituted other actions based on diversity of citizenship. See n. 1, *supra,* p. 4.

[27] *Robinson* v. *Difford,* 92 F. Supp. 145 (E.D. Pa.); *Speed* v. *Transamerica Corp.,* 99 F. Supp. 808 (D. Del.); *Northern Trust Co.* v. *Essaness Theatres Corp.,* 103 F. Supp. 954 (N.D. Ill.). See also *Llanos* v. *United States,* 206 F. 2d 852 (C.A. 9), certiorari denied, 346 U.S. 923, where the court rejected an argument similar to that advanced by the instant petitioners (Pet. Br. 16-17), that the giving of promissory notes in exchange for personal loans did not involve sales of securities within the meaning of the 1933 Act because Congress never intended the statute to be applicable to personal transactions such as these.

the ruling below will "flood the federal courts" [28] with local disputes apparently does not extend to local controversies involving mailed *written* misrepresentations, rather than *oral* misstatements. They readily concede that even under their proffered construction, "Section 12(2) would still apply to a purely local transaction where a prospectus was sent through the mails within a single state and was used to sell a security" (Pet. Br. 24). Petitioners offer no satisfactory reason why Congress would want to afford a federal civil remedy for written misrepresentations even as respects a "local controversy", but deny one for the same misrepresentations if made orally; and, of course, it seems clear enough that Congress never contemplated such a distinction.

The legislative history of Section 12(2) supports our construction. The language of Section 12(2) first appeared in the House bill. H. R. 5480, 73d Cong., 1st Sess. (1933). While different in terminology, the civil liabilities provisions of the Senate bill were substantially as broad, but contained no "jurisdictional language". [29] The omis-

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[28] No such "flood" has resulted from the decision in *Schillner v. H. Vaughan Clarke & Co.*, 134 F. 2d 875 (C.A. 2), handed down in 1943, which the court below followed. Certainly, the remedy for an overworked federal judiciary does not lie in misconstruction of remedial federal legislation, but elsewhere.

[29] In relevant part, the Senate bill read as follows (S. 875, 73d Cong., 1st Sess. (1933), 77 Cong. Rec. 2979, 2981):

> * * * Every person acquiring any security by reason of any false or deceptive representation made in the course of or in connection with a sale or an offer for sale or distribution of such securities shall have the right to recover any and all damages suffered by reason of such acquisition of such securities from the person or persons

sion seemingly resulted from the preoccupation of the Senate draftsmen with the basic purpose of providing a federal civil remedy for misrepresentation and fraud in the sale of securities.[30] Notwithstanding the omission, in the Conference Report the managers on the part of the House, comparing the two provisions, characterized them as "substantially similar".[31] It described the section as one imposing "civil liability for using the mails or the facilities of interstate commerce to sell securities * * * by means of representations which are untrue or are misleading by reason of omissions of material facts."[32] Thus the jurisdiction limits were applied to the sales, not to the representations.

The congressional debates provide further support for the construction adopted by the court below. Members of Congress showed particular concern about the inadequacy of state "blue sky" laws to deter or prevent fraudulent securities transactions, and about the need for employing the comprehensive powers of Congress in this regard.[33] The inability of individual states to cope adequately with the problems presented by the securities industry which, as a whole, is interstate in character, admittedly was the primary factor in bringing

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signing, issuing, using, or causing, directly or indirectly, such false or deceptive representation, jointly or severally * * *.

[30] See S. Rep. No. 47, 73d Cong., 1st Sess. (1933), p. 1.

[31] Conference Report, H. Rep. No. 152, 73d Cong., 1st Sess. (1933), pp. 26-27.

[32] *Ibid.*

[33] See 77 Cong. Rec. 2912, 2914, 2918, 2920, 2930-31, 2935, 2953-54.

about federal legislation; and petitioners highlight this in the portions of the legislative debates referred to in their brief. Some of their other references, relating to the exclusion of intrastate transactions, have no pertinency here since they were concerned with the registration provisions of the statute.[34] None of petitioners' references involve specific discussion of the statutory program in Sections 12(2) and 17(a) with respect to fraudulent and deceptive sales. There are, however, positive indications in the legislative history that Congress intended to make full use of its constitutional powers in dealing with such sales. During the course of the House debates, Representative—and former Solicitor General—Beck pointed out that those powers were twofold: "One, the power of the United States over post roads, and therefore the mails; and the other, the commerce clause." "The power over the mails," he thought, "is a much broader power than the power over interstate commerce." 77 Cong. Rec. 2935. In the course of the Senate debate, Senator Fletcher, Chairman of the Senate Committee which held hearings on the bill, also explained that the pro-

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[34] For example, the quotations from the Committee reports on page 23 of petitioners' brief.

Other quotations from the floor debates relied upon by petitioners (Pet. Br. 20-21) appear to be casual and generalized statements made without consideration of the statutory provisions relating to the use of the mails—statements which petitioners themselves cannot consistently accept as accurate in view of petitioners' agreement as to the sufficiency of intrastate mailings of written misrepresentations. Compare Mr. Justice Jackson's observation in *Schwegmann Bros.* v. *Calvert Distillers Corp.*, 341 U.S. 384, at 396.

posed statute was jurisdictionally based not only on the commerce clause but also on the fact that "the securities also move in the mails". 77 Cong. Rec. 2983. This is in harmony with Senator Norbeck's later comment that "in the pending bill the authority of the Government rests largely on the fact that the mails are used in the transaction of this business * * *" 77 Cong. Rec. 3223. These jurisdictional bases appeared in various portions of the Senate bill but, as we have already pointed out, jurisdictional language inadvertently was omitted from the civil liabilities provisions of the Senate proposal. The foregoing indicates, however, that the Senate intended to exercise comprehensively any postal powers Congress possessed. Such comprehensive exercise of jurisdiction, of course, would include transportation of the security or other uses of the mails not involving communication of the misrepresentations complained of. When Senator Wheeler observed that the mail fraud statute (18 U.S.C. 1341) already covered the situation of oral misrepresentations followed by a mailing of the security itself or other material (77 Cong. Rec. 2983), Senator Fletcher remarked that the proposed legislation does not "in any wise restrict or limit or weaken the laws already on the statute books," but rather "strengthens and broadens the authority to proceed in such instances." 77 Cong. Rec. 2983, 2984.

In articles published shortly after passage of the Act, eminent authorities read Section 12(2) as did the court below. See, *e.g.*, Douglas and Bates,

The Federal Securities Act of 1933, 43 Yale L. J. 171, 177, 183, n. 51, 209, n. 213 (1933); Frankfurter, *The Federal Securities Act: II,* 8 Fortune 53, 108 (1933); Dean, *The Federal Securities Act: I,* 8 Fortune 50, 102 (1933); see also Dodd, *Amending the Securities Act—The American Bar Association Committee's Proposals,* 45 Yale L. J. 199, 223 (1935). It was not until years later that language inaccurately paraphrasing Section 12(2) crept into some court dicta, thus affording a semblance of authority for a construction which offered wide opportunities for circumvention of the statute.

This brings us to the cases under Section 12(2). All but one of the court holdings support the construction urged herein. In addition to the holding below of the Court of Appeals for the Fifth Circuit, there is the ruling of the Court of Appeals for the Second Circuit in *Schillner* v. *H. Vaughan Clarke & Co.,* 134 F. 2d 875. In that case defendants sold stock by oral misrepresentations made to plaintiffs at their home. The only use of the mails was to deliver the stock certificates from defendants' office in Philadelphia, Pa., to plaintiffs' home in Rome, New York. In rejecting defendants' argument that Section 12(2) had no application because the misrepresentations had not been transmitted by mail or by use of interstate facilities, Judge Swan stated (134 F. 2d, at 877):

> We do not think that this is the inevitable, or even the most natural, meaning of the statutory language. Liability to repay the consideration received is imposed upon any person who

> "sells a security * * * by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication" of the untrue or misleading character described in the section. To accept appellant's construction would render the phrase "oral communication" of most limited application because the section would then reach only interstate telephone calls or conversations where the parties might be talking across a state line. *It would seem much more likely that Congress intended to make the statute applicable if one sells a security by use of the mails, even though the seller's untrue or misleading statement is communicated orally and intrastate.* [Emphasis added.]

In *Moore* v. *Gorman,* 75 F. Supp. 453 (S.D. N.Y.), defendants made oral misrepresentations and concluded an oral agreement of sale in Philadelphia. Defendants' agent, however, made a round trip by rail between Philadelphia, Pa., and New York City, N. Y., in order to deliver the securities and bring back plaintiff's check in payment. Dedefendants moved to dismiss on the ground, *inter alia,* that no misrepresentation was transmitted by interstate facilities. The motion was denied on the authority and reasoning of the *Schillner* case.

Recently, in *Fratt* v. *Robinson,* 203 F. 2d 627, the Court of Appeals for the Ninth Circuit had occasion to consider the "jurisdictional language" of Section 12(2) in passing upon a similar contention that Rule X-10B-5 under the 1934 Act was inap-

plicable where the misrepresentations were oral and intrastate. In rejecting that construction of Rule X-10B-5, Judge Stephens also reviewed the holdings and dicta under Section 12(2) and expressed agreement with the view adopted in the *Schillner* and *Moore* cases (203 F. 2d, at 634, n. 20).

On the other hand, petitioners' proffered construction finds support in the decision of the Court of Appeals for the Seventh Circuit in *Kemper* v. *Lohnes,* 173 F. 2d 44, and in certain paraphrasings of Section 12(2) by some other courts which, with one possible exception, are clearly dicta. In none of these cases is there any analysis of the statutory considerations. In the *Kemper* case the complaint alleged that, in response to defendant's newspaper advertisement, plaintiff advised defendant by mail of his interest in purchasing certain stock; that defendant replied by mail arranging for a meeting; and that at this and subsequent meetings defendants made the material misrepresentations which induced the sale. Both parties were residents of Chicago and everything took place in that city. The court held Section 12(2) inapplicable. It assumed the answer to the critical question at the very outset when it started with the premise that Section 12(2) requires that the misrepresentations be transmitted either by use of interstate facilities or of the mails. Since an oral misrepresentation obviously cannot be transmitted through the mails, the court concluded that the statutory phrase "oral communication" must refer only to misrepresenta-

tions communicated through interstate facilities—*e.g.*, "telephone conversations * * * in interstate commerce and perhaps broadcasts by radio" (173 F. 2d, at 45-46). Likewise, there is no supporting discussion for the early statement in *Siebenthaler* v. *Aircraft Accessories Corp.*, CCH Fed. Sec. L. Rep. ¶ 90,122 (W.D. Mo. 1940), and early dicta in two other cases. In the *Siebenthaler* case there is a brief statement in the numbered conclusions of law that Section 12 was not applicable, "there being no prospectus and no oral communication involving the means or instruments of transportation or communication in Interstate Commerce". The actual holding in that case is not clear; for there was no positive finding of any fraudulent misrepresentation or omission.[35] In *Murphy* v. *Cady*, 30 F. Supp. 466 (D. Me., 1939), affirmed, 113 F. 2d 988 (C.A. 1, 1940), certiorari denied, 311 U.S. 705, plaintiff recovered on proof of oral misrepresentations communicated by interstate telephone.[36] Similarly, in *Independence Shares Corp.* v. *Deckert*, 108 F. 2d 51 (C.A. 3, 1939), reversed without discussion of point, 311 U.S. 282, the alleged mis-

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[35] The *Siebenthaler* case has been criticized because its "narrow construction" would "seriously impair the scope of the section, and must be abandoned if the section is to be of any real use to injured investors." Comment, *Civil Liability under the Federal Securities Act*, 50 Yale L. J. 90, 101 (1940).

[36] See, however, the later observation of the Court of Appeals for the First Circuit in *Crooker* v. *S.E.C.*, 161 F. 2d 944, 947 (1947): "Any person who sells a security in interstate commerce by means of an untrue or misleading statement of material facts in a prospectus or oral communication is subject to civil liability under § 12(2), and to criminal penalties as provided in §§ 17 and 24."

representations were transmitted by use of interstate instrumentalities. At a later stage of the proceedings in that case, the court observed: "The gravamen of the cause of action * * * is the misleading of the purchaser." *Pennsylvania Co.* v. *Deckert*, 123 F. 2d 979, 984 (C.A. 3). The *Kemper* decision has not been followed. Rather, as shown above, it has since been disapproved by two courts of appeals.

For the reasons stated, the court below correctly decided that Section 12(2) applies where the mails have been used in the fraudulent sale, even though the particular misrepresentations were oral and intrastate. We turn now to the question whether the mailings here alleged were mailings in the sale of the securities.

II. The Alleged Uses of the Mails to Deliver the Documents Essential to the Investment Contracts Are Mailings in the Sale of the Securities under Section 12(2) of the Act.

We agree with the court below that the alleged uses of the mails to consummate the sales by delivery of the documents which were essential parts of the investment contracts, *viz.*, the warranty deeds and the care contracts, sufficed to bring the transactions within the ambit of Section 12(2) (R. 54). Petitioners, on the other hand, assert that the transactions were complete when the contracts were agreed upon and the deeds made out and recorded,[37] so that the delivery of the deeds through the mails conferred no additional rights (Pet. Br. 12). This argument starts from a false premise and follows

[37] See note 4, *supra*, p. 6.

it to a false conclusion. We are not dealing here with "a simple real estate sale" (Pet. Br. 16). The court below held that the transactions alleged in the complaint involved the sale of investment contracts of which the transfer of the title to land was but a part. The securities consist of the entire agreements between the sellers and the buyers, including specifically the "care contracts". It appears from the dates recited in the complaint that these contracts were not actually completed during the initial interviews, but were filled in and dated at a later time and then forwarded through the mails to the investors. It is futile therefore to speculate on whether sales of land are completed by the recording of deeds under the real property law of Texas, for the simple reason that we are not concerned with the transfer of title to land as such.[38] While we do not regard it as essential to the applicability of Section 12(2) that completion of the care contracts was thus delayed—in view of the broad statutory definition of the term "sell" and the court decisions construing Sections 12(2) and 17(a) as applicable where the mails are used to deliver stock certificates after completion of the initial contract, to which we refer below—there is no doubt that, in the instant case, the sales transactions were not completed until the documents were in fact delivered through the mails.

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[38] If the real property law of Texas were deemed relevant, it is significant that delivery of a deed is deemed essential to transfer title to land. Vernon's Tex. Rev. Civ. Stat. Ann. Art. 1288; *Steffian* v. *Milmo National Bank*, 69 Tex. 513, 6 S.W. 823; *McGowen* v. *Montgomery*, 248 S.W. 2d 789 (Tex. Civ. App.).

Section 12(2) applies to any person who "sells a security * * * by the use * * * of the mails * * *" The terms "sale" and "sell" are defined by Section 2(3), 15 U.S.C. § 77b(3), to "include every contract of sale or *disposition of, attempt* or offer *to dispose of* * * * a security * * * for value * * *" (emphasis added). This language on its face covers the use of the mails in effectuating any portion of the sale transaction, including consummation by delivery of the security.[39] This has been the uniform construction of the comparable language of Section 17(a)—"in the sale of any securities * * * by the use of the mails"—and of the similar language of Rule X-10B-5—"by the use of * * * the mails * * * in connection with the purchase or sale of any security." See the cases set forth in pp. 24-26, *supra*.

The cases holding that Section 12(2), also, requires only that any of the stated federal instrumentalities be used in the sale transaction likewise agree that it is sufficient if the mails are used in consummation of the transaction. Thus, as previously indicated, the use of the mails or instrumentalities of interstate commerce to deliver the securities has been held sufficient not only by the court below, but also by the Court of Appeals for the Second Circuit in *Schillner* v. *H. Vaughan Clarke & Co.*, 134 F. 2d 875, and by a federal district court in *Moore* v. *Gorman*, 75 F. Supp. 453 (S.D. N.Y.). See

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[39] The definition, it was contemplated, would operate "broadly." See H. Rep. No. 85, 73d Cong., 1st Sess. (1933), p. 11.

also *S.E.C.* v. *Wimer*, 75 F. Supp. 955 (W.D. Pa.), holding that delivery of securities by mail from one state to another involves a "sale" at the place of delivery within the meaning of the venue provisions of Section 22(a) of the Act, 15 U.S.C. § 77v(a). In the *Moore* case, *supra*, the court also referred to the use of instrumentalities of interstate commerce to collect payment for the securities sold there as a basis for jurisdiction under Section 12(2). 75 F. Supp., at 456-57.

The sole contrary judicial authority, to our knowledge, is a statement in *Gross* v. *Independence Shares Corp.*, 36 F. Supp. 541 (E.D. Pa.), that the use of the mails to deliver the security is not a use in the sale of the security within the meaning of Section 12(2).[40] Judge Bard pointed to the fact that the registration provisions of Section 5(a)(2), 15 U.S.C. § 77e(a)(2), expressly rendered unlawful, among other things, the use of the mails "for delivery after sale" of an unregistered security. The absence of any express reference to "delivery" in Section 12(2), he thought, indicated that such use of the mails would not be suf-

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[40] The court held sufficient other mailings in that case—mailings of payment notices and other material designed to induce investors to continue contracts relating to securities sold under an installment payment plan. It should be observed that, in the present case, the complaint similarly alleges that the periodic billings on the care contracts contain misrepresentations intended to induce respondents to continue payments pursuant to the investment arrangements and to deter withdrawals therefrom. If the complaint can be viewed as alleging sales which partially, at least, were on an installment basis, these mailings would appear sufficient even under petitioners' thesis.

ficient under that section. The *Gross* statement was considered and rejected by the Court of Appeals for the Second Circuit in the *Schillner* case (134 F. 2d, at 877-78). As Judge Swan pointed out, whereas Section 5(a)(2) refers to mailings to make "delivery after sale", Section 5(a)(1) renders unlawful the use of the mails to "sell" an unregistered security, without any reference to delivery. Both civil recovery provisions of Section 12 likewise simply use the word "sells". Section 12(1) imposes civil liability upon any person who "sells" in violation of the registration requirements of Section 5. Section 12(2) imposes liability upon one who "sells" by misrepresentations or half-truths. If the word "sells" is construed consistently in Section 12 to exclude delivery after sale, Section 12(1) would then be limited in scope to violations of only part of Section 5(a). This, Judge Swan reasoned, would be clearly contrary to the intent of Congress, particularly in light of the fact that the statute imposes criminal liability for violation of any part of Section 5(a). The word "sells", he concluded, must be taken to include delivery of the security if Section 12(1) is to be given its full meaning; and there was no warrant for giving a different meaning to the same word as used in Section 12(2). Moreover, he pointed out, such construction fully accords with the broad definition of the term "sell" in Section 2(3) which includes the *"disposition"* of the security.

Judge Swan recognized that since Section 5(a)

(2) differentiated between the use of the mails to sell and the use of the mails to deliver after sale, the word "sell" may have narrower meaning in Section 5(a)(2) than in Section 12. The broad Section 2 definition applies "unless the context otherwise requires". The context of the registration provisions of Section 5 is different, as we have already shown. The appropriate reference in the construction of Section 12(2) is the basic statutory definition and not the language employed in Section 5. The *Gross* statement, followed to its logical end, would also apply to the anti-fraud provisions of Section 17(a), and perhaps Rule X-10B-5 under the 1934 Act, so as to render insufficient under those provisions uses of the mails to effect or obtain delivery of securities sold or purchased by misrepresentation and fraud. We have previously shown that this is contrary to the uniform holdings of the courts. See pp. 24-26, *supra*.

For the reasons stated, we believe it clear that the court below also properly decided that the complaint alleges uses of the mails in the sale of the securities within the meaning of Section 12(2).

CONCLUSION

The judgment below should be affirmed.

Respectfully submitted,

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MARCH, 1954.

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Decisions Per Curiam.

No. 423. BENTSEN ET AL. *v.* BLACKWELL ET AL. Certiorari, 346 U. S. 908, to the United States Court of Appeals for the Fifth Circuit. Argued March 9, 1954. Decided March 15, 1954. *Per Curiam:* The argument having developed the undesirability of deciding the questions in this case on the pleadings, the writ of certiorari is dismissed. *Paul A. Porter* and *Milton V. Freeman* argued the cause for petitioners. With them on the brief was *Jackson Littleton*. *Edward Holland McIlheran* argued the cause for respondents. With him on the brief was *Garland F. Smith*. By special leave of Court, *John F. Davis* argued the cause for the Securities and Exchange Commission, as *amicus curiae*, urging affirmance. With him on the brief were *Solicitor General Sobeloff*, *William H. Timbers*, *Alexander Cohen* and *Henry L. Stern*. Reported below: 203 F. 2d 690.